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DISCRIMINATION IN HOME MORTGAGE LENDING

HEARING

BEFORE THE

SUBCOMMITTEE ON
CONSUMER AND REGULATORY AFFAIRS

OF THE

COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

ONE HUNDRED FIRST CONGRESS

FIRST SESSION

ON

STATISTICAL EVIDENCE OF DISCRIMINATION CURRENTLY AVAILABLE AND RECOMMENDATIONS FOR WHAT MORE NEEDS TO BE DONE TO ELIMINATE DISCRIMINATION IN HOME MORTGAGE LENDING

OCTOBER 24, 1989

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DISCRIMINATION IN HOME MORTGAGE LENDING

TUESDAY, OCTOBER 24, 1989

U.S. Senate,
Committee on Banking, Housing, and Urban Affairs,
Subcommittee on Consumer and Regulatory Affairs,
Washington, DC.

The subcommittee met at 10 a.m., in room SD-538 of the Dirksen Senate Office Building, Senator Alan Dixon (chairman of the subcommittee) presiding.

Present: Senators Dixon, Garn, Riegle, Kerry, Bond, Cranston, Graham, and D'Amato.

OPENING STATEMENT OF SENATOR DIXON

Senator Dixon. Good morning, ladies and gentlemen. We're here today to investigate discrimination, particularly racial discrimination, in home mortgage lending.

Last spring, Senator Chris Dodd of Connecticut and I, with Senator Riegle's support, added a provision to the savings and loan bill. That law required the Federal bank and the thrift regulators and HUD to report to the Congress on two points: first, statistical evidence of discrimination currently available; and, second, recommendations for what more needs to be done to eliminate discrimination in home mortgage lending.

Those reports are now ready. Our first panel of witnesses will present the findings. Our second panel will present community group perspectives on the reports, as well as their own experiences from around the country with trying to remedy discrimination.

I'd like to make a few comments before they begin. The report from the Office of Thrift Supervision found that nationally black mortgage loan applicants are rejected roughly twice as often as white applicants. Further, the Federal Reserve reported that studies in various cities around the country all conclude that predominantly black neighborhoods receive fewer home purchase loans than comparable white neighborhoods, even after accounting for differences in income and other economic variables. All the regulators hastened to add that these statistics don't prove discrimination.

Well, I'm not a statistician, but when blacks are getting their loan applications rejected twice as often as whites and, in some cities, it's three and four times as often, I conclude that discrimination is part of the problem.

I don't know the best way to address this problem, yet. I helped pass a law so that you, the regulatory agencies, would be required to provide Congress with your best advice. If I were you, I would not call most of these reports, "my best advice."

And I would not claim that because I found few violations, there must be widespread compliance with anti-discrimination laws. The very same circular reasoning would argue that regulators found few violations because they are not enforcing the law sufficiently.

I call upon everyone here today and everyone involved in lending and housing to put forward their best advice on how we can end this discrimination.

Ladies and gentlemen, it's 21 years since passage of the Fair Housing Act. Fifteen years since the Equal Credit Opportunity Act was passed in the Congress; and 11 years since the Community Reinvestment Act became the law of this land, and still we have discrimination in lending. The problem today is not lack of laws, in my view, it is lack-luster enforcement.

It may be that discrimination today is more institutional than intentional. It may be more prejudice against a neighborhood than against a person; more a matter of giving white applicants the benefit of the doubt than showing black would-be borrowers the door. But, it is still wrong. It still has the same harmful effect. And like the segregation of the years past, ladies and gentlemen, it still must be stopped.

Now, I'm privileged to see here at the Committee meeting, indicating I think the importance of this hearing, the distinguished chairman of this committee and the distinguished ranking member. And I'm honored to have the Chairman, Senator Riegle of Michigan, here. And I'm delighted to hear your statement.

OPENING STATEMENT OF SENATOR RIEGLE

Senator Riegle. Thank you very much, Chairman Dixon. Let me just say at the outset how much I appreciate the strong leadership you're giving this Subcommittee. When we talked early in the year about establishing this Subcommittee with multiple set of purposes, today's subject was one of those purposes.

And you said at that time that it was your intent to move into these areas with great energy, and you've done exactly that. And I want to commend you for your leadership for the strong statement you've made this morning, and for the work of your Subcommittee.

This is a very important subject here today. It is a sad and shocking fact that in this day and age we still face mounting evidence of mortgage discrimination from around the country. It is clearly a problem that needs to be addressed and solved, and there really is no excuse for further delay.

I'm pleased to note that the Financial Institutions Reform, Recovery and Enforcement Act of 1989, the savings and loan reform legislation, contains several provisions which we were able to work on together that are addressed at the mortgage discrimination problem, including very important amendments to the Community Reinvestment Act and a substantial overhaul of the Home Mortgage Disclosure Act.

I want to just say parenthetically that not often do we have an opportunity like that to make some substantive changes in law, but the Savings and Loan Reform package gave us that opportunity and we took advantage of it to make these changes.

And so we think they will be helpful as we go forward.

It is my hope that those provisions will, in fact, be a big help in the fight against mortgage discrimination. And if there are other things that we ought to be doing, I want to hear and consider the recommendations of this Subcommittee, Senator Dixon, as you complete your work, so that we can decide what further steps may be appropriate.

I'm also delighted to indicate that we have today with us a couple of important Michigan witnesses on today's second panel.

One is Dr. Arthur Johnson, who is the vice president for community relations and chairman of the Detroit chapter of the NAACP. He will be presenting testimony jointly with Mr. Bernard Parker, who is the executive director of the Community Resources Program of Operation Get Down in Detroit, which is a community-based organization of excellent reputation involved in a variety of programs, including a very important cooperative food program.

Dr. Johnson and Mr. Parker cochaired the Detroit Ad Hoc Coalition on Fair Banking Practices, which has managed to reach settlements with all of the major banks in the Detroit area under their leadership.

I think it's a very significant case example of progress being accomplished through that process. And I want very much for them to be able to apprise the committee of what has been done and perhaps provide some guidance to other communities that have not yet been able to make the strides that we feel we have at this point in the City of Detroit.

The committee is very honored by their presence, and I want to extend a welcome to them, and yield back to you, Mr. Chairman.

Senator DIXON. I want to thank you very much, Chairman Riegle. And we are delighted to have this distinguished panel of witnesses here this morning. May I suggest that the ground rules will be that we will hear from each of you for 7 minutes. I won't be absolutely strict about the 7 minutes, but I ask you to indulge me because, shortly after that, I do get strict.

And we are going to take the gentlemen first and the lady last. I understand that that is something that is satisfactory to Ms. Fitts. And so the distinguished panel is John P. LaWare, a member of the Board of Governors of the Federal Reserve System; C. Austin Fitts, Assistant Secretary for Housing, Department of Housing and Urban Development, Commissioner, Federal Housing Administration; Mr. Jonathan Fiechter, Senior Deputy Director of Supervisory Policy for the Office of Thrift Supervision, our new name for that agency; Dr. Robert J. Herrmann, Senior Deputy Comptroller for Bank Supervision Policy, the Office of the Comptroller of the Currency; and Mr. John F. Bovenzi, Deputy to the Chairman, Federal Deposit Insurance Corporation.

And we thank you all for indulging us by your presence here this morning. And if it's all right with everybody concerned, I think we'll go left to right with you, Mr. LaWare, excluding Ms. Fitts and coming back to her to conclude.

Senator DIXON. Mr. LaWare.

JOHN P. LaWARE, MEMBER, BOARD OF GOVERNORS, FEDERAL RESERVE SYSTEM, WASHINGTON, DC

Mr. LAWARE. I appreciate this opportunity to discuss with the committee the Federal Reserve's findings in its recent study of mortgage lending discrimination, which was prepared in response to provisions of FIRREA.

First, I want to tell you that this is an issue about which my fellow Governors and I have the utmost concern.

Congress has made very clear in the Fair Housing Act, the Equal Credit Opportunity Act and the Home Mortgage Disclosure Act that ensuring equal access to housing, including the credit necessary to buy a home, is a fundamental tenet of national public policy.

The Congress has also charged the Federal Financial Regulatory agencies with enforcing those laws, and we take that charge very seriously.

Our study explains that the Federal Reserve has in place a comprehensive examination program to enforce compliance with these and other laws safeguarding the interests of the consumer in a very complex financial marketplace.

The report explains how examiners compile information about credit applicants, comparing the characteristics of those accepted and those rejected, and analyzing the distribution of loans actually made.

Examiners determine what the bank's stated lending standards are and how consistently they have or have not been applied.

They interview bank lending personnel and seek input from people in the community about the bank's reputation as a fair lender and its perceived credit practices.

Banks are required to take corrective action in accordance with an established Board enforcement policy when substantive violations are found.

A parallel to our examination program, the Federal Reserve's Consumer Complaint Specialists provide professional help in investigating and securing appropriate remedies in instances where consumers' credit rights have been violated.

Complaints alleging discrimination against a protected class of loan applicant—that is to say, women, minorities, persons receiving public assistance payments, and others—receive particularly careful attention, although I must say they are very few in number.

I'm proud of the way that these programs are structured to meet our enforcement responsibilities and even more so of the efforts of our staff at the Board and at the Reserve Banks to implement them.

Yet, they have some inherent limits, as our report points out.

For example, it is generally very difficult to make a clear determination that deliberate discrimination has occurred, given that there may well be legitimate business reasons for the imposition by a bank of credit standards, conditions or prices which may vary over time.

In the one to 3 weeks typically spent on a bank premises, examiners may also not be able to detect the, I hope, isolated instances in which certain applicants are discouraged, perhaps in very subtle ways, before an application is actually filed.

Just as importantly, persons who have been discriminated against may not come forward, perhaps because they are unaware of their rights under the law or the recourse available, or simply because they are intimidated by the process.

The issue of discrimination in mortgage lending has been brought to the fore recently by several well-publicized studies focusing on the relationship between the racial composition of neighborhoods and home purchase lending in those neighborhoods.

Those studies are probably correct in identifying disparities in the number of mortgages extended in mostly white and mostly minority areas with roughly the same income. Yet, these studies stop short of the conclusion that deliberate racial discrimination is the only, or even the most significant, cause for such differences.

In many instances, for example, loans in those same minority neighborhoods for home improvement significantly out-number home improvement loans in white neighborhoods.

And we believe that there are other important factors at work in the real estate market that influence lending patterns. For example, the frequency of housing turnover; the traditionally high level of activity by mortgage bankers and finance companies, and the suitability of different loan products offered by commercial banks and thrifts; the influence of appraisers and real estate brokers; and factors other than income which affect, finally, credit-worthiness.

The distribution of loans in any community is a result of the interaction of many diverse variables affecting demand and supply. While discrimination could play a role, to conclude that these studies prove discrimination without thoroughly examining the other factors present seems questionable.

Our job is to ensure that the 1,100 or so State member banks of the Federal Reserve System, representing about 8 percent of commercial banks in the country, provide people fair access to credit. We have tried conscientiously to do so through our examination and complaint-handling work and the results seem to indicate these efforts, as measured by the extent of State member bank compliance with fair lending laws, have been largely successful.

It is not our job to allocate credit. That is not the charge that the Congress has given us. I do not wish to imply that we think that all banks are aggressively meeting the mortgage credit needs of their communities. And in some isolated cases, we may not have been able to detect an act of illegal credit discrimination, for the reasons that I described a minute ago.

In some instances, we have found that the banks we regulate could certainly stand to improve their outreach to less well-served segments of their market and to develop loan products genuinely responsive to local needs.

And we have worked with them to do so in our enforcement of the Community Reinvestment Act. In those cases, we believe we are not dealing with overt discrimination but more probably with a lack of understanding on the part of bankers of the communities they serve and of community development lending techniques.

We may also be dealing with a deeply rooted distrust of banks by some members of the minority community, and a reluctance on the part of those individuals to deal with banks.

On the other hand, I think the very existence of our examination program would have caused any bank which might be inclined to ignore the law to think again.

And I feel that, though our examiners might miss the isolated case of improper conduct by an individual bank employee, they would not miss bank policies or systematic behavior which resulted in illegal discrimination.

Personally, I find it difficult to reconcile the notion that there is widespread racial discrimination in mortgage lending with the fact that bankers want to make loans; not only to strengthen their financial prospects for the short-term, but to ensure that the community in which they operate thrives.

In my more than 30 years experience as a banker, I found the industry strongly committed as a matter of self-interest to make every sound loan possible, given that lending is the single most important source of income for most banks.

Perhaps the bias of individual bankers may have clouded their judgment on occasion but, in the main, I think that the institutional commitment to doing business where it makes economic sense will win out over prejudice.

And in pursuit of that goal, I have to mention to you some recommendations that were included in our report and are being considered by the Financial Institutions Examination Council. And we hope that some of these will have early implementation.

First of all, mortgage review boards, which are set up in communities with representatives from the lenders as well as from the community. I know that this process has worked well in Boston, by my own experience. And the possibility of having those set up in other standard metropolitan statistical areas makes, perhaps, some sense. That's one thing that we're considering.

We are also considering showing each bank its mortgage lending profile using the new HMDA data which we are in the process of gathering as a result of the amendments made in FIRREA. And that kind of a profile would tend to bring to management's attention, as part of the examination report, just what their performance is and what the patterns of their lending are.

Senator DIXON. I wonder, Mr. LaWare, if you could supply to us the rest of your recommendations in view of the time constraints.

Mr. LAWARE. I'd be happy to. Thank you.

FFIEC staff is also considering sharing the results of examiner contacts with community members with FFIEC member agencies and developing an educational pamphlet for lenders that will address prohibited practices under the anti-discrimination laws. Board staff is also looking at the possibility of developing a pamphlet for consumers that would describe a mortgage loan applicant's rights under the antidiscrimination laws to ensure that members of a protected class have equal access to mortgage credit. Finally, in light of the recent changes to the Home Mortgage Disclosure Act, Board staff will be undertaking a review of our loan discrimination examination and training procedures.

Senator DIXON. We appreciate very much your testimony.

Mr. LAWARE. Thank you, Mr. Chairman.

[The complete prepared statement of John P. LaWare follows:]

For release on delivery
10 a.m., E.D.T.
October 24, 1989

Statement by

John P. LaWare

Member, Board of Governors of the Federal Reserve System

before the

Subcommittee on Consumer and Regulatory Affairs

of the

Committee on Banking, Housing, and Urban Affairs

United States Senate

October 24, 1989

SUMMARY OF TESTIMONY

The report, which is the subject of the testimony, was submitted to the Congress by the Board of Governors of the Federal Reserve System pursuant to section 1220 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). Section 1220 required the Board and the other Federal Financial Institution agencies to report to the Congress on their findings on the extent of discriminatory lending practices by mortgage lenders subject to their regulation or supervision (in the Board's case, state member banks) using currently available loan acceptance and rejection statistics. In addition, the reports were to provide recommendations for appropriate measures to assure nondiscriminatory lending practices.

The Board does not currently have mortgage loan acceptance or rejection statistics of the type contemplated by section 1220. Consequently, it was unable to provide the requested analysis. Nevertheless, the Board was able to draw some conclusions about the possible extent of discriminatory conduct in the mortgage lending activities of state member banks as a result of Federal Reserve System's consumer affairs program.

There are two anti-discrimination laws for which the Board has enforcement responsibilities with respect to state member banks--the Fair Housing Act and the Equal Credit Opportunity Act. The Fair Housing Act, among other things, prohibits discrimination in a residential real estate-related transaction against any person because of race, color, religion, sex, national origin, handicap or familial status. The Equal Credit Opportunity Act prohibits creditor practices that discriminate against an applicant because of race, color, religion, national origin, sex, marital status or age (provided the applicant has the capacity to contract); the fact that all or part of the applicant's income derives from a public assistance program; or the fact that the applicant has in good faith exercised any right under the Consumer Credit Protection Act.

Federal Reserve System efforts to detect loan discrimination by state member banks began in 1977 and include both a consumer compliance examination effort and consumer complaint effort. The consumer compliance examinations are comprehensive, scheduled at regular intervals, and are conducted by examiners at the Reserve Banks who are specially trained in consumer affairs and civil rights examination techniques. The Board and each of the Reserve Banks maintain staff who work primarily with complaints from consumers who feel they have been treated unfairly by a state member bank. The Board's staff provides general guidance and oversight to the Reserve Banks in both areas.

The examination procedures for detecting loan discrimination during a consumer compliance examination are quite detailed. They take on average almost 19 hours per examination to complete, and result in a comprehensive assessment of the institution's lending practices.

Overall, the number and nature of the violations of the Equal Credit Opportunity Act (Regulation B) and the Fair Housing Act discovered during our compliance examinations suggests that state member banks are in substantial compliance with the requirements of both Acts. We do not find policies or practices that suggest that individual state member banks take the race of an applicant into account when making a credit decision.

In recent years the staff of the Federal Reserve System has conducted or reviewed several research studies that have examined the relationship between the racial composition of neighborhoods and residential mortgage lending. This work has been based on information obtained from records of actual loans granted rather than from loan application records.

The studies do not draw definitive conclusions about the existence or extent of racial discrimination. They are nonetheless useful because they identify the presence of differential lending patterns across neighborhoods and thus focus attention on these matters. The existence of these disparities, regardless of their cause, should at the very least prompt mortgage lenders to review their marketing and outreach efforts as well as their product offerings in minority neighborhoods.

The Board was also asked to provide recommendations for appropriate measures to assure nondiscriminatory lending practices. In light of the recent amendments contained in the FIRREA to the Home Mortgage Disclosure Act, which will assist in developing a more complete and accurate picture of mortgage lending practices than is possible today, we have no proposals for new additional legislation. We do, however, have several initiatives that are currently under review by the Board staff or subcommittees of the Federal Financial Institution Examination Council (FFIEC), which show promise.

* * * * * * * * * * * * * * * *

Mr. Chairman, I appreciate this opportunity to appear before this Senate Subcommittee to present the Federal Reserve Board's view on the extent of state member banks' compliance with federal laws which prohibit discrimination in mortgage lending. In particular, my testimony will summarize the Board's "Report on Loan Discrimination," which was submitted to the Congress pursuant to Section 1220 of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA).

Section 1220 required the Board and the other federal financial institution supervisory agencies to report to the Congress on their findings on the extent of discriminatory lending practices by mortgage lenders subject to their regulation or supervision (in the Board's case, state member banks) "based on a review of currently available loan acceptance and rejection statistics." In addition, the reports were to provide recommendations for appropriate measures to assure nondiscriminatory lending practices.

Although the Board has a comprehensive compliance examination program to ensure that state member banks comply with the Equal Credit Opportunity Act and the Fair Housing Act, it does not currently have mortgage loan acceptance or rejection statistics of the type contemplated by Section 1220. Consequently, we were unable to provide the requested analysis. Recent amendments to the Home Mortgage Disclosure Act will require certain state member banks as well as other lenders to report this type of data, but it will not be available until the fall of 1991.

Nevertheless, the Board was able to draw some conclusions about the possible extent of discriminatory conduct in the mortgage lending activities of state member banks as a result of the Federal Reserve System's consumer compliance examination program. In addition, some information was provided by our consumer complaint program. Finally, we have followed closely the concerns over disparities in the amount of residential mortgage lending between minority and non-minority areas as detailed by studies in Atlanta, Cleveland, Detroit, and Boston - the latter conducted by the Federal Reserve Bank of Boston. These studies provide useful, but limited, insight into the issue.

Antidiscrimination Laws

Two laws directly prohibit discrimination in mortgage lending--the Fair Housing Act and the Equal Credit Opportunity Act. These two laws are complementary in some important respects relating to mortgage lending. For example, both set forth criteria which lenders may not consider when making credit decisions.

The objective of the Fair Housing Act is to help assure nondiscriminatory practices in all aspects of the housing market. Consequently, it applies to a wide range of persons involved in the sale or rental of housing and regulates many aspects of residential real estate-related transactions. With regard to mortgage credit, the Fair Housing Act makes it unlawful for mortgage lenders to discriminate in a residential real estate-related transaction against any person because of race, color, religion, sex, national origin, handicap or familial status. The primary impact of the Act with regard to state member banks is to require equal treatment of applications for mortgage loans from members of a protected class.

The Equal Credit Opportunity Act and the Federal Reserve System's Regulation B, which implements the Act, are designed to assure the nondiscriminatory availability of all types of credit, including mortgage loans, to all creditworthy applicants. The Act and the Regulation prohibit creditor practices that discriminate against an applicant because of race, color, religion, national origin, sex, marital status or age (provided the applicant has the capacity to contract); the fact that all or part of the applicant's income derives from a public assistance program; or the fact that the applicant has in good faith exercised any right under the Consumer Credit Protection Act. In addition, there are certain other important requirements in the Act and Regulation relevant to mortgage lending procedures which are designed in different ways to further the overall purpose of promoting the nondiscriminatory availability of credit.

The Board has broad rule-writing responsibility for the Equal Credit Opportunity Act, but very limited enforcement authority. The Congress directed the Board to prescribe regulations to carry out the purpose of the Act for covered lenders--including, for example, all banks, other depository institutions, and mortgage lenders. In contrast, the Board is given administrative enforcement responsibility for only state member banks.

The Fair Housing Act, itself, does not give the Board any rule-writing or enforcement authority. The Department of Housing and Urban Development and the Attorney General are designated as the responsible federal agencies with regard to such matters. Nevertheless, the procedures for the Board's consumer compliance examination program include checking for state member bank compliance with the Fair Housing Act under our general authority to assure that banks are complying with federal law.

Before I explain the Board's enforcement program, I would like to briefly explain some characteristics of state member banks to indicate the type of financial institutions on which our program is focussed and on which our conclusions are based.

State member banks are relatively small in size and number and many are rural. As of December 31, 1988, there were 1,109 state member banks out of a total of 13,418 commercial banks in the United States (approximately 8 percent). They hold about 14 percent of total deposits held by commercial banks in this country and 90 percent of state member banks have total assets of less than $500 million. Over 45 percent of state member banks are not located in an MSA (metropolitan statistical area).

Moreover, state members banks are not a significant presence in the mortgage lending area. Analysis of the most recent aggregated Home Mortgage Disclosure Act statistics (1987) indicate that state member banks originated less than three percent of all home purchase loans reported.

Federal Reserve Board's Consumer Affairs Program

The Board first established a specialized consumer compliance examination program in 1977. This program required that the twelve Reserve Banks around the country conduct examinations of state member banks to determine compliance with consumer protection legislation by using a cadre of specially trained examiners. The scope of these examinations specifically included the Equal Credit Opportunity and Fair Housing Acts. From the beginning, the examiners were instructed to place special emphasis on violations involving potential discrimination of the kind prohibited by these statutes.

In 1979, the Board reassessed its enforcement responsibilities in the areas of consumer affairs and civil rights and made several changes to its consumer affairs program. This included increased training for examiners in detecting discriminatory lending practices. Changes were also made in the System's processing of consumer complaints. It also placed increased emphasis on investigating serious complaints such as allegations of loan discrimination.

In 1981, the Board re-emphasized state member bank responsibilities under the Equal Credit Opportunity Act and the Fair Housing Act, and put the banks on notice that the Board would vigorously enforce them. This reminder took the form of a Policy Statement which stated that failure to comply with certain provisions of the acts were viewed by the Board to be particularly serious and would require retroactive corrective action.

Federal Reserve System efforts to detect loan discrimination by state member banks focus on the consumer compliance examination effort. Consumer compliance examinations are conducted by examiners at the Reserve Banks who are specially trained in consumer affairs and civil rights examination techniques. The Board and each of the Reserve Banks maintain staff who work primarily with consumer complaints. The Board's staff provides general guidance and oversight to the Reserve Banks in both areas. The Federal Reserve System's consumer compliance examinations are scheduled at regular intervals, and are comprehensive. As a result, the Board has been able to maintain a high-quality examination program over the years.

Each state member bank is examined on a regular basis. The Board's examination frequency policy calls for an examination to be scheduled every eighteen months for a bank with a satisfactory record. Banks with exceptional records can be examined every two years. Those banks with less than satisfactory records are to be examined every six months or every year, depending on the severity of their problems.

The Board believes that expecting a bank examiner to master both the "safety and soundness" and consumer affairs/civil rights aspects of bank examinations is not practical given the existing complexities of both areas which continue to increase. Consequently, the Federal Reserve has developed a separate career path for consumer affairs examiners equivalent to that of commercial examiners at the Reserve Banks. The Board provides special training to these examiners.

On average, checking for compliance with the anti-discrimination laws takes almost 19 hours per examination to complete, and results in a comprehensive assessment of the institution's lending practices.

The procedures focus primarily on comparing the treatment of members of a protected class with other loan applicants. First, the bank's loan policies and procedures are reviewed. This is done by reviewing bank documents, as well as interviewing loan personnel. During this phase, the examiner will seek to determine, among other things, the bank's credit standards. After the examiner has identified those standards, he or she will then contrast those standards with a judgmental sampling of actual loan applications, especially applications received by the bank from members of a protected class. This means that the examiner is looking at the same information that the bank used to make its credit decision, including such things as credit history, income, and total debt burden. If an instance is discovered where those standards appear not to have been used, it could be an indication of prohibited discrimination. This would provide the basis for a discussion with lending personnel and/or more intensive investigation. Finally, an overall analysis of the bank's treatment of applications from members of protected classes is conducted to determine whether there are any patterns or individual instances where such members were treated less favorably than other loan applicants.

One other aspect of the examination procedures is an analysis of the geographic distribution of the bank's credits.

Two ways in which this can be done is by plotting the location of the bank's accepted and rejected loans in a selected category on a map, and/or by use of Home Mortgage Disclosure Act data, if available. These data are then cross-referenced to census data, or other available information which identifies low- and moderate-income and minority neighborhoods. The geographic analysis has two functions. First, it may highlight lending practices evidenced by a geographic pattern that negatively impacts4 on members of a protected class. Second, it is used in evaluating the bank's performance under the Community Reinvestment Act.

Another regular part of the examination includes conversations initiated by the examiner with persons in the community knowledgeable about local credit needs. The examiners will routinely ask about public perceptions of the availability of credit to minorities and low- and moderate-income persons. This information may suggest that a particular area of the bank needs additional scrutiny and may provide crucial insights into how the bank is serving the credit needs of its local community, particularly those individuals in the community protected by the antidiscrimination statutes.

There are, however, two significant reasons why these procedures, extensive as they are, may not provide absolute assurance that there have been no individual instances of discrimination.

First, state member banks, as most lenders, provide a certain amount of flexibility in their credit standards. This reflects the fact that variations are normally found in each applicant's request for credit. In addition, numerous factors are used to establish creditworthiness (e.g., the amount and reliability of income, employment history, other debts, credit history, adequacy and availability of loan collateral, length of time at present residence, the existence and nature of deposit relationships), and this increases the difficulty in determining with any degree of certainty whether a member of a protected class was denied credit due to the fair application of credit standards or to discrimination.

Second, the pricing, structure and even availability of loans also vary. These variations are primarily due to business considerations which might include, for example, the perceived risk of loan default, usury or other legal requirements, the bank's cost of funds at any given time, and liquidity considerations. Such factors often make it more difficult to determine whether those who obtained credit, albeit on different terms, were treated equally.

For these two reasons, making conclusive judgments as to whether any particular variation is due to legitimate business reasons or discrimination is an inexact and difficult task. Discrimination can occur in many subtle ways, and it seldom leaves a visible audit trail. As a consequence, we can rarely be certain that discrimination has occurred, and we seldom make this formal finding. However, it is not uncommon for examiners to fully explore a questionable variation through conversations with bank personnel. This aspect of the examination process may play a substantial role in sensitizing lenders to the issue of discrimination.

As part of the examination procedures, examiners are instructed to review bank practices and policies regarding pre-application contact with potential customers. In this regard, it is often difficult for compliance examiners to determine, with certainty, what type of interaction may have occurred between potential applicants and the bank before an application is received. If applicants are being discouraged from submitting an application, and there is no documented evidence of such treatment, it is possible the examiner will not learn of this improper bank conduct unless the affected applicants come forward.

Overall, the number and nature of the violations of the Equal Credit Opportunity Act and the Fair Housing Act discovered during our compliance examinations suggest that state member banks are in substantial compliance with the requirements of both Acts. While there are several procedural requirements of Regulation B and the Fair Housing Act which some state member banks have not followed, as detailed in our report, these violations do not directly involve the antidiscrimination provisions.

In summary, we do not find policies or practices that suggest that individual state member banks take the race of an applicant into account when making a credit decision. Moreover, the very fact that bank personnel know that examiners will be closely scrutinizing their behavior, through review of bank records, probably has a considerable influence on helping to discourage discriminatory conduct by individual employees.

Home Purchase Lending Disparities by Race

In recent years the staff of the Federal Reserve System has conducted or reviewed several research studies that have examined the relationship between the racial composition of neighborhoods and residential mortgage lending. Copies of these materials, which pertain to Atlanta, Boston, Cleveland, and Detroit were included in our report.

The Federal Reserve work has all been based on information obtained from records of actual loans granted (either from data obtained pursuant to the Home Mortgage Disclosure Act or from local government property records) rather than from loan application records. Consequently, these studies do not specifically address the question raised in section 1220, which is the extent of mortgage lending discrimination revealed in a review of loan application and disposition records. Nevertheless, the studies do provide some insights into the relationships between race and home lending.

The studies show:

(1) that there are differences in the number and dollar volume of conventional home purchase and home improvement loans extended to borrowers in different neighborhoods;

(2) that, after accounting for differences in neighborhood income levels, in the number of housing units across neighborhoods, as well as in other selected control variables, areas with predominantly black populations receive fewer home purchase loans, but more home improvement loans, from commercial banks and thrift institutions than similar predominantly white neighborhoods, and

(3) that a significant portion of the home purchase finance extended in predominantly black neighborhoods is supplied by non-depository institutions, such as mortgage companies, and, except for Boston, most of these loans are either government-insured or guaranteed (apparently high home prices in Boston has precluded some potential loan applicants from using FHA-insured financing in recent years).

Each of the studies discusses various factors which may account for these loan patterns. For example, the Boston study describes in some detail the complex interaction of demand and supply in both the housing and mortgage markets that combine to jointly determine the distribution of home purchase loans across different neighborhoods. Because the distribution of loans reflects the joint determination of supply and demand factors, many of which are closely related to each other, interpreting the significance of any particular variable is extremely difficult.

The studies, however, do not draw definitive conclusions about the existence or extent of racial discrimination. They are nonetheless useful because they identify the presence of differential lending patterns across neighborhoods and thus focus attention on these matters. For example, the finding that mortgage bankers and other non-depository sources of finance are a dominant source of credit in many predominantly minority areas has raised questions about the adequacy of bank and thrift institution marketing and community outreach in these communities. In addition, the observation that FHA-insured financing is heavily used in minority middle-income neighborhoods suggests that depository institutions could garner a larger share of the home loan market in these neighborhoods if more of them offered FHA-insured loans or similar low downpayment, privately insured conventional mortgage alternatives. Finally, the existence of these disparities, regardless of their cause, should at the very least prompt mortgage lenders to review their marketing and outreach efforts as well as their product offerings in minority neighborhoods. We have recently stressed this responsibility in a joint agency policy statement on the Community Reinvestment Act.

Recommendations

The Board was also asked to provide recommendations for appropriate measures to assure nondiscriminatory lending practices. In light of the recent amendments contained in the FIRREA to the Home Mortgage Disclosure Act and the Community Reinvestment Act, we have no proposals for new legislation.

The amendments to the Home Mortgage Disclosure Act will--

(1) extend coverage of the Home Mortgage Disclosure Act to essentially all types of mortgage lenders;

(2) require disclosure of data on the disposition of loan applications (in addition to data on loans originated and purchased); and

(3) require disclosure of data on the race, sex, and income level of borrowers and applicants.

These amendments will provide new information about the characteristics of loan applicants which will enhance the ability of examiners to determine whether a lender's credit standards are being fairly applied. Also, the extension of the coverage of HMDA to include essentially all mortgage lenders will provide a more complete context in which to judge a bank's mortgage lending efforts.

FIRREA amends the Community Reinvestment Act to provide that after July 1, 1990, the written evaluation of a depository institution's record of meeting the credit needs of its local community made by the institution's regulatory agency must be disclosed to the public. Public disclosure will increase the significance of the evaluation of the bank's performance with that Act because it will likely lead to increased dialogue between banks, examiners, and community groups.

The Board believes that the new enhancements to these two statutes will assist in developing a more complete and accurate picture of mortgage lending practices than is possible today, and that no additional legislation is necessary. There are, however, several additional initiatives under review by the Board's staff or subcommittees of the Federal Financial Institution Examination Council (FFIEC), which are referred to in the report.

In closing, I would like to emphasize the Board's commitment to vigorously enforcing the antidiscrimination laws for which it has responsibility. Home ownership is a important part of the American dream and we all want to assure that every American, regardless of race, is treated fairly if he or she pursues that goal. To this end, we think our enforcement program helps provide confidence that state member banks are providing mortgage credit on a nondiscriminatory basis.

Senator DIXON. Mr. Fiechter, we're delighted to have you here.

JONATHAN FIECHTER, SENIOR DEPUTY DIRECTOR OF SUPERVISORY POLICY, OFFICE OF THRIFT SUPERVISION, WASHINGTON, DC

Mr. FIECHTER. Thank you, Mr. Chairman, Senator Riegle.

I'm pleased to appear this morning to discuss our report on loan discrimination. The Office of Thrift Supervision is deeply committed to assuring that savings associations uphold the provisions of the nondiscrimination laws and regulations, develop affirmative policies and procedures and treat all loan applications fairly.

We are very concerned about any meaningful disparities identified in either our analysis or other credible studies that suggest that minority and nonminority loan applicants are not being treated uniformly by savings associations.

The subcommittee is no doubt aware that there have been recent studies that strongly suggest disparate treatment of minority loan applicants by financial institutions.

These studies and their implications cannot be ignored. In our view, they must be analyzed carefully and thoroughly and the results must be reflected in the agency's examination programs.

We are presently building a strong and capable compliance examination program that emphasizes the fair lending laws and regulations.

The Federal Home Loan Bank Board and now Office of Thrift Supervision have had a loan application register and data submission report system since 1978. Statistics on acceptance and rejection rates available from that system do indicate that there are disparities in mortgage home rejection rates between black and white applicants.

On a nationwide basis, as you mentioned in your opening remarks, the rejection ratio indicates that blacks are rejected for mortgage loans approximately twice as often as whites. Even greater disparities exist in several major metropolitan statistical areas.

This finding, however, only suggests the possibility of unequal treatment. It does not indicate that savings associations are necessarily engaged in racial discrimination. The data itself offers no information as to the financial position of any loan applicant, nor does it provide any data on an individual savings association's credit or underwriting criteria.

The data does, however, serve a very important function in the examination process by identifying areas for hypothesis testing by examiners.

Our nondiscrimination examination procedures are designed to use the available system data along with other important demographic information about a savings association's community to identify disparities in the treatment of applicants on prohibited bases.

From these disparities, the examiner formulates hypotheses for further testing. For example, the data might indicate that black mortgage loan applicants are rejected much more frequently than white mortgage loan applicants. The examiner would draw samples of black and white mortgage applicants and compare the two against each other and to the savings association's underwriting criteria.

The purpose would be to determine whether an individual or class of applicants was treated in a discriminatory manner.

The nondiscrimination procedures are part of the new OTS Compliance Examination Program. As approved in January 1989, this new program utilizes a separate force of specially-trained examiners to conduct examinations for compliance with the nondiscrimination laws and regulations, the Community Reinvestment Act, the consumer protection laws and regulations, and a number of public interest-related matters.

This program will be fully implemented by the end of 1990. At this time, our district offices are actively recruiting individuals for compliance examiner positions while conducting separate compliance examinations with generalist examiners.

The new specialized Compliance Examination Program is a significant first step towards reaffirming this agency's commitment to compliance matters.

Compliance by savings associations with laws and regulations is one of the major missions of this agency, and we intend to assure that proper attention is paid to this area.

We would be the first to admit that we have not devoted the necessary amount of emphasis in recent years to the development of a compliance examination program.

We recognized that shortcoming in 1987 and are well on our way to making a compliance program a significant supervisory strength.

In addition to the new examination program, there are other possible initiatives to enhance enforcement of the fair lending laws. As we noted in our October 9 report to this Committee, the Task Force on Consumer Compliance of the FFIEC is developing various options for possible consideration by the FFIEC's principals.

Among the options, in addition to the two mentioned by Governor LaWare, under consideration by the task force is the approach of using testers as a means of assessing to what extent institutions are engaged in illegal prescreening of mortgage applicants.

Another idea is to have the agencies utilize a "SWAT" team approach with each agency conducting examinations of all of their respective institutions in a given geographic area at roughly the same time when available data suggests the possibility of a disproportionate ratio of loan distribution among low-to moderate-income and/or minority applicants.

Senator DIXON. What kind of an approach did you call that, Mr. Fiechter?

Mr. FIECHTER. A "SWAT" team. Where all of the agencies bring examiners in simultaneously.

I'd like to emphasize that neither the FFIEC nor any of its individual members has yet endorsed any of the options currently under consideration by the Consumer Compliance Task Force.

Rather, the staff of the task force has felt obliged to consider the full range of options in order to provide the FFIEC principals with as much information as possible.

Mr. Chairman, we believe that we have taken strong affirmative steps toward renewing our commitment to the compliance area. We postured ourselves to tackle the challenge of assuring that all loan applicants have equal access to the credit markets.

We are looking forward to the benefits that specialization in the compliance field will surely bring to us.

This agency simply will not tolerate discriminatory practices by any of the savings associations we regulate.

Thank you. I'd be happy to try and answer any questions you might have.

[The complete prepared statement of Jonathan Fiechter follows:]

STATEMENT OF
JONATHAN L. FIECHTER
SENIOR DEPUTY DIRECTOR FOR SUPERVISION POLICY
OFFICE OF THRIFT SUPERVISION, U.S. DEPARTMENT OF THE TREASURY
BEFORE THE SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS
OF THE SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
OCTOBER 24, 1989

Mr. Chairman, I would like to thank the Subcommittee for the opportunity to testify on the Office of Thrift Supervision's (OTS) "Report on Loan Discrimination" submitted pursuant to Section 1220 of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA). My testimony will discuss the significant findings of that report and its recommendations, the nondiscrimination procedures used by OTS examiners, and our new and expanded program for enforcing the fair lending laws and regulations.

SIGNIFICANT FINDINGS

Before discussing the findings contained in our report, it is important to briefly describe our system for the collection of mortgage loan acceptance and rejection data. Since September 1978, savings associations have been required to maintain a loan application register in which is recorded information derived from written applications for dwelling-related loans. Savings associations are required to maintain at each decision center a separate, current, readily accessible register for one-to-four family dwelling loans, mobile home loans, and home improvement/equipping loans. A decision center is an office where decisions are made to approve, on terms requested or as changed, or take any adverse action on applications for dwelling-related loans. The registers include information identifying an application, any resulting loan, the disposition of an application, the date of disposition, and the Metropolitan Statistical Area, census tract, and zip code (as applicable) of the subject property. The registers also contain information identifying the race, sex, marital status and age of an applicant, along with loan data such as the interest rate and term.

On a semi-annual basis, savings associations are required to aggregate certain register information on "data submission reports" (DSRs) for transmittal to OTS District Offices and to OTS Washington. OTS then prepares a series of DSR reports for use by its District Offices. In addition to reports on individual savings associations and decision centers, a series of macro-level reports are produced. These reports show the aggregate number of loan applications handled by the reporting savings associations by loan type on a national, District, and Metropolitan Statistical Area basis.

The reports identify the total number of applications, the number granted, the number rejected/denied, the number withdrawn, and the number pending at the close of the reporting cycle. The data is further subdivided into four categories: type of census tract; race; sex; and, marital status. The reports also convert the raw numbers on the disposition of applications to percentages.

Finally, the reports list various ratios based on the data. The ratios compare, for example, the number of loans granted in minority census tracts to the number of applications received and pending in such tracts. One of the purposes of the ratios is to highlight for examiners areas of greatest disparity that should be addressed during an examination.

OTS staff has reviewed available data from the agency's Loan Application Register and Data Submission Report System (LARS/DSR) and is aware that there are some differences in the acceptance and rejection rates between minority and nonminority applicants, as well as differences on the basis of census tract characteristics. These differences, in and of themselves, do not indicate that savings associations are discriminating on a prohibited basis, as the data system does not enable one to draw such a conclusion. The data does, however, raise questions that examiners must address as part of the examination process.

The data indicates, for example, that black mortgage loan applicants have been rejected by reporting savings associations at roughly twice the rate as white mortgage loan applicants on the national level. The data does not provide any information as to the creditworthiness or economic circumstances of any particular applicant nor does it offer any information about a particular lender's credit or underwriting criteria. Moreover, comparable data from commercial banks, credit unions, and other financial institutions are not available for analytical purposes. The significance of the differences cannot be ignored, but can only be explored and explained through vigorous field examinations that thoroughly analyze a given savings association's policies, procedures, lending programs and criteria. In addition to the routine examination process, we are using this data as a basis for conducting special nondiscrimination examinations where appropriate.

There are some aspects of the system which arise from some arbitrary designations as to census tract characteristics that pose difficulties in interpreting the data. For example, under the system, a "substantially minority" census tract is a tract where 25 percent or more of the population is comprised of minority residents. With this definition in mind, even if the population in a census tract is 75 percent white, the data would characterize application activity in that census tract as involving a minority populace.

The OTS LARS/DSR system was designed in 1978 as a tool to assist examiners in carrying out the agency's nondiscrimination enforcement responsibilities. The system focuses on a lender's decisions on individual applications and on the characteristics of the individual applicants. In addition, it provides information on the geographic location and census tract characteristics of the subject property. This emphasis on individual application data and the disposition of an application helps examiners determine whether particular lenders are engaging in discriminatory actions affecting particular applicants or classes of applicants as well as whether lenders are discriminating against geographic areas. The data must be used in connection with other information gathered through the examination process relating to the demographics of a savings association's community. Information about the minority population and percent of owner-occupied housing, for example, help give further meaning to the DSR statistics.

It is critical to understand that the data does not represent prima facie evidence or proof that a lender has engaged in discriminatory practices or has discriminated against a particular individual. The data merely points out potential disparities in the treatment of classes of applicants based on race, sex, marital status, and property location characteristics. Examiners use the data to formulate hypotheses about the treatment of certain classes of applicants and test those hypotheses with actual application information.

Statistics showing a disproportionate number of loan denials from minorities, women, or other protected classes, or a disproportionate rejection rate in minority areas, raise questions which savings associations should be called upon to answer or which should be analyzed by examiners in their review of loan application registers in the examination process. For example, a high denial rate for minorities may be the result of a vigorous outreach program rather than attributable to discriminatory loan policies and standards or the uneven application of nondiscriminatory policies and standards. Similarly, a high approval rate for minorities, particularly when coupled with a low volume of applications, may be indicative of prescreening. While firm conclusions normally cannot be drawn from the DSR data, questionable flows and patterns are identified and explored as part of the examination process.

OTS is deeply concerned about any meaningful disparities that point to potential differences in the way members of protected classes are treated as compared to others in the lending process. While our data, and our analysis of it, does not manifest proof of credit discrimination, our new examination program is designed to make full use of available data and make certain that such matters are thoroughly addressed. I want to assure the Subcommittee that we are committed to investigating alleged instances of discrimination and monitoring the activities of savings associations in this area.

RECOMMENDATIONS TO ASSURE NONDISCRIMINATORY LENDING PRACTICES

FIRREA Changes

The FIRREA made substantial changes to strengthen nondiscrimination enforcement, all of which the Federal Home Loan Bank Board strongly endorsed during the legislative process. The extension of the Home Mortgage Disclosure Act requirements to independent mortgage companies and the expansion of that Act's provisions to require the reporting of applicant data and the inclusion of data on race, income, and gender of mortgage loan applicants will significantly improve the HMDA data collection system that now exists. For institutions regulated by OTS, these changes will have little impact as the FIRREA changes were patterned to a great degree after our own loan application register system. The examination process will be augmented by the inclusion of income data in particular and examiners should be able to develop more exacting and refined hypotheses for testing during the nondiscrimination examination.

As a matter of fact, the OTS loan application register system requirements exceed those of the amended HMDA and we intend to continue mandating that savings associations maintain some of the nonduplicative data for use by our examiners.

The FIRREA also requires the development of a uniform CRA rating system to be used by the federal financial institution regulatory agencies. These CRA ratings will be made public along with a CRA evaluation of the institution's performance. An institution's performance under the nondiscrimination laws is, and will continue to be, a significant part of the CRA evaluation. These changes will serve to heighten a financial institution's awareness that it is, in essence, more publicly accountable for its CRA performance.

FFIEC Activities

The Director of OTS' Division of Compliance Programs is a member of the Task Force on Consumer Compliance of the Federal Financial Institutions Examination Council (FFIEC). This task force promotes policy coordination and uniform enforcement of consumer laws by the five agencies represented on the FFIEC (the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Reserve Board, the OTS, and the National Credit Union Administration). The task force also identifies and studies problems concerning consumer compliance matters.

The Task Force has been actively seeking ways in which the agencies could enhance institution's understanding of and compliance with the Equal Credit Opportunity Act and the Community Reinvestment Act. The Task Force has identified several opportunities that it believes could be pursued to further the agencies' enforcement efforts with the nondiscrimination requirements. The Task Force will be seeking the advice of the FFIEC regarding these matters in the near future. These enhancements include:

Fair Lending Audit: This is a means of providing the agencies with information as to whether or not illegal discriminatory treatment of potential mortgage applicants is a contributing factor to the higher rejection rates of minority applicants and to the racial patterns in the geographic distribution of mortgages made by financial institutions. The audit would employ the use of "testers" to provide better information on the troubling questions of whether or not discrimination exists in the pre-application stages.

"SWAT" Team Examination Effort: This exercise would enable the regulators to determine the presence or absence of discriminatory lending practices in areas where there is an indication that a disproportionate ratio of loan distribution exists among low- to moderate- income and/or minority residents. The agencies represented on the FFIEC would agree to conduct examinations in all their respective major institutions in targeted areas of the country within a certain period of time and share their findings. Clearly, coordination between the agencies would enhance the volume of available information on lending activities in a given geographic region.

OTS strongly believes that our primary vehicle for strengthening enforcement with the nondiscrimination laws is the establishment of a separate, specialized examination force to conduct compliance examinations. Dedicated specialists who are trained in the compliance field can pay greatly increased attention to this area. Consequently, we are committed to having our new compliance examination program fully implemented by the end of 1990. Our new program is explained later in my testimony.

OTS also believes that other significant participants in the lending process should be subject to strengthened enforcement activities. Discrimination in the real estate markets can take place long before a potential home buyer even approaches a financial institution for a mortgage loan. For example, potential home buyers can be "steered" to certain neighborhoods based on racial or other prohibited factors by real estate agents. Although a part of the overall process is linked to financial institutions, there are others involved in the process whose activities might be studied by the Congress, such as real estate agents and brokers, appraisers and private mortgage insurers.

NONDISCRIMINATION EXAMINATION PROCEDURES

Our examination procedures for the nondiscrimination laws and regulations include those for the Equal Credit Opportunity Act and its implementing Regulation B, the Fair Housing Act, the Home Mortgage Disclosure Act and its implementing Regulation C, and procedures for monitoring compliance with our own agency requirements. The OTS Compliance Activities Handbook contains a separate section on each of these laws that include examination objectives, procedures, and checklists. The examination procedures for each of these laws are designed to determine that savings associations do not discriminate in the granting of credit on any prohibited basis, and to determine that savings associations are in compliance with the law. The nondiscrimination examination process relies on Home Mortgage Disclosure Act data, information derived from consumer complaints, the savings association's policies and procedures, and the LARS/DSR system.

Information from the LARS/DSR system is used extensively in the examination process, as described herein. Prior to using the data in a substantive manner, examiners review the registers and the DSRs for accuracy. This is basically a technical routine where the examiner assures that the institution has properly compiled the DSR reports from the registers and that the registers are maintained as required. This is referred to as Segment I of the nondiscrimination review.

Segment II begins the substantive examination process and uses the registers and the DSRs to determine whether any discrepancies based on applicant or property characteristics are apparent. The objective of this review is to determine if lending practices or policies have a disproportionate impact on any race, sex, marital status, type of census tract, or property age group. There are four main parts to this review:

1. The examiner determines if applications reflect illegal prescreening or other factors which would limit the inflow of applications from any protected group. This is accomplished by comparing the savings association's application levels for each group to other savings associations in the same area. Low rejection rates or application levels may indicate prescreening.

2. The examiner determines if the savings association rejects applications from any group with a disproportionate frequency or its acceptance levels are disproportionately lower for one or more groups. The DSR is used to determine, for any group, if there are disproportionate numbers of loan denials, higher withdrawal rates, or delays in handling applications.

3. The examiner determines if the savings association has adequate economic justification for any policies or practices which have a disproportionately negative effect based on applicants' ages.

4. The examiner determines whether any discrepancies between groups are large enough to warrant further study.

Assuming that there are such discrepancies, the examiner proceeds to Segment III of the procedures. In this segment, the examiner tests any hypotheses raised during the steps performed above. For example, the examiner may notice, from a review of the register and DSR information that black applicants are denied more frequently than white applicants for mortgage loans. The examiner would then review a representative sample of loan or application files. The sample should include at least 15 files from the group with the less favorable treatment (black applicants) and 15 from the group with the more favorable treatment (white applicants). The examiner then determines whether the reasons for the rejections (or other less favorable treatment) are consistent with the institution's underwriting criteria and whether they are uniformly applied to all applicants and to all areas.

OTS COMPLIANCE EXAMINATION PROGRAM

Brief History

Prior to early 1989, the Board's compliance examination responsibilities (which include, among other things, enforcement of the nondiscrimination and fair lending laws such as the Fair Housing Act, Equal Credit Opportunity Act, and Community Reinvestment Act) were carried out as part of the safety and soundness examinations of savings associations. These examinations were performed by generalist examiners on a 6 to 18 month time frame depending upon the financial condition of an association. Frankly, as the thrift crisis heightened during the 1980's and substantial examination resources needed to be devoted to financial matters, compliance examination responsibilities became a secondary priority. It was not until after 1985, when the examination staff was removed from Civil Service and transferred from the Board to the Federal Home Loan Banks that the agency was able to make plans to enhance its compliance examination program.

It should be noted, however, that before the thrift crisis and its impact on the Board's ability to appropriately staff its ranks to adequately fulfill its examination responsibilities as it would have liked, the Board had an aggressive and well-respected examination approach to nondiscrimination and compliance matters. The Board's LARS/DSR system made it virtually unique among the federal financial institution regulators.

Key Components of the New Compliance Examination Program

In October 1987, the System's Office of Regulatory Policy, Oversight and Supervision (later changed to the Office of Regulatory Activities) established the Division of Compliance Programs to provide a focus for the development of a national compliance examination program. This division's primary mission is to develop a national examination and supervisory program to address compliance matters. The division's responsibilities include overseeing compliance with the traditional consumer laws and regulations, such as the Truth in Lending Act, nondiscrimination requirements, the Community Reinvestment Act, and a number of other public-interest laws such as the Bank Secrecy Act.

The Division of Compliance Programs has two broad goals. First, the division provides educational services to assist savings associations in understanding and complying with laws and regulations. In this regard, the division published a manual entitled, "Compliance: A Self-Assessment Guide" in July 1988. This guide is designed to provide helpful information to savings associations in developing viable compliance programs and in conducting and reporting compliance reviews. The guide also includes a Policy Statement that strongly suggests that every savings association establish a compliance program commensurate with its size and complexity. It is this agency's firm belief that every savings association has a business responsibility to develop and maintain an ongoing compliance program. The guide was distributed at no cost to every savings association under our jurisdiction. Additionally, nearly 1,000 copies have been sold to interested parties. The division has also introduced a series of brochures addressing regulatory problem areas. The first brochure in the series addressed the Bank Secrecy Act and was released in May 1989.

Second, the division administers an enforcement program which directs OTS' compliance examination and supervisory responsibilities. A separate examination program for the compliance area was approved in January 1989. Probably the most significant element of the new compliance program involves our decision to utilize examiners that specialize in the compliance laws and regulations. These examiners receive specialized training in the laws and regulations covered within the scope of the compliance examination.

Our compliance training at this time consists of a two-week basic level school. The first session of this school was conducted this past July and the second session is scheduled for December. Six basic school sessions are scheduled for 1990, with an estimated enrollment of 30 examiners at each session. Participants in this school receive roughly 12 hours of classroom instruction on the nondiscrimination laws and regulations plus an additional 12 hours on the Community Reinvestment Act. In early February 1990 we will begin planning our secondary level compliance school and anticipate holding the first session of that school before the end of the year.

The division also completed and distributed copies of a new "Compliance Activities Handbook " This effort represents the first time that the agency has had all of its examination procedures pertaining to the nondiscrimination, consumer, and public-interest laws and regulations in a handbook devoted exclusively to them. The new handbook provides examiners with specific guidance as to the conduct of compliance examinations, textual information on each law and regulation contained in the compliance examination program, and examination objectives, procedures, and checklists. In addition to serving as a primary examination tool, the handbook is provided to savings associations where it serves as an educational centerpiece.

Examinations under the specialized program are conducted on a frequency schedule driven by the lower of either the CRA or compliance rating assigned at the previous examination. The interval between examinations can range between 6 and 24 months - the lower the rating, the more frequently a savings association would be examined. At this time, ratings assigned during the examination for both CRA and compliance are based on a 5-point scale with "1" representing the most favorable performance and "5" the poorest. Ratings of "1" and "2" reflect satisfactory performance while "3," "4," and "5" signify progressively deepening degrees of unsatisfactory performance and supervisory concern.

At the conclusion of a compliance examination, the District office prepares a separate, comprehensive examination report written primarily for the benefit of a savings association's board of directors and senior management. The report is all narrative and is designed to be consultative and educational. Report content is geared toward areas in need of improvement and is tailored to each individual institution.

The new compliance examination program should be fully staffed and implemented by January 1, 1991. Currently, examiners are being selected and assigned to the compliance area at each District office, training is being provided, and separate examination reports are being prepared. The full specialized compliance program may well be completely operational sometime before the 1991 effective date.

CONCLUSION

OTS is committed to identifying and eliminating discrimination and to encouraging nondiscriminatory practices in the operations of savings institutions. The vigorous enforcement of the fair lending laws of this country is a major responsibility of this agency. One of the principal OTS missions is to ensure compliance with the full range of laws and regulations to which thrifts, their officials and their shareholders are subject. We believe that we have taken important affirmative steps, as explained herein, to assure that the savings associations we regulate will refrain from discriminatory practices. Those who do not will be subjected to the full extent of our enforcement authority.

Senator DIXON. Thank you very much, Mr. Fiechter.

Mr. Robert J. Herrmann, Senior Deputy Comptroller for Bank Supervision Policy, the Office of the Comptroller.

We're delighted to have you here, Mr. Herrmann.

ROBERT J. HERRMANN, SENIOR DEPUTY COMPTROLLER FOR BANK SUPERVISION POLICY, OFFICE OF THE COMPTROLLER OF THE CURRENCY, WASHINGTON, DC

Mr. HERRMANN. Thank you, Mr. Chairman, Senator Riegle, Senator Kerry. In my testimony today, I will discuss how the OCC enforces fair lending laws and regulations. Specifically, in the context of illegal discrimination in mortgage lending.

Mr. Chairman, in the interest of time, I'd like to submit my detailed written statement for the record.

Senator DIXON. Thank you. And in the case of every witness, may I announce that your complete statements will be reproduced in the record, and have been read by the Chair. We appreciate them.

Mr. Herrmann.

Mr. HERRMANN. Thank you, Mr. Chairman.

I'd like to spend my time discussing just a few of the important points the written testimony makes.

The OCC's supervisory role in examination procedures primarily ensures that home buyers who formally apply to national banks for mortgage credit are not treated discriminatorily on bases prohibited by law. Illegal discrimination in home finance can be particularly difficult to detect and measure because it can occur in so many different stages in the attempt to secure mortgage financing.

Home buyers may encounter illegal discriminatory behavior by sellers and their agents, by lenders, by appraisers, by insurers or by advertisers, all of whom may directly or indirectly affect financing or prospective purchases.

Buyers may even steer themselves to lenders perceived as more receptive to their needs and away from lenders believed to be discriminatory.

Stated another way, potential customers can be affected by illegal discriminatory behavior at any one of four stages:

During preliminary discussions with realtors, brokers and so forth on where to seek financing; when inquiring about mortgage loans with a bank's personnel; and at the time of filing an application with a bank; or during the bank's credit decision process.

Activities that occur prior to a bank's involvement are outside of our authority and ability to enforce as bank regulators.

We can do little to detect illegal discriminatory behavior if it occurs prior to the bank's receiving a written application because prior to that point, there is no tangible evidence.

Under our compliance program, we annually examine institutions representing approximately 40 percent of national banking system assets.

Examinations include an independent assessment of the level of compliance with fair lending laws. Examiners provide bank management and its board of directors not only a report of specific violations, but an assessment of the bank's own systems to detect and prevent problems.

When examiners find problems that a bank system did not detect, we require bank management to take corrective actions and we monitor the implementation of those actions.

To assess a bank's performance, examiners review bank policy, procedures and underwriting standards.

Examiners also evaluate a sample of loan applications to determine if a bank's decision to either grant or deny credit appears consistent with its stated policy.

If discrepancies appear, especially on bases that cannot be used as criteria for loan decisions—a good example is race—Examiners expand their review of application files to ensure that illegal discriminatory practices do not exist.

OCC's consumer complaint information system might be an indicator of discrimination, but there have been very few discrimination-related complaints filed with our agency.

Of over 37,000 written complaints that we received between January 1987 and August 1989, a 32-month period, only 16 alleged racial discrimination complaints were received.

After investigating each of the complaints, no violations of law were cited. Since April 1987, the OCC conducted 3,437 consumer compliance examinations. During these exams, we cited 381 violations subject to the policy statement for the enforcement of ECOA and the Fair Housing Act in 239 banks.

We did not find any violations of the Fair Housing Act or indications of illegal discrimination in real estate lending. The vast majority of these violations dealt with inadequate or incomplete adverse action notices.

Regarding the violations cited, banks were required to conduct file searches for the previous 24-month period and correct both past and present violations.

Bank management was required to revise policies and procedures to ensure that violations would not recur.

The OCC does not rely solely on examinations to encourage banks to meet their fair lending obligations. Compliance with Fair Lending laws also includes an assessment of the bank's activities related to the Community Reinvestment Act.

One of the assessment factors included in the CRA's implementing regulation requires examiners to review a bank's policies to determine if there are any underlying practices that discourage applications for types of credit offered by the bank.

As appropriate, examiners conduct meetings with local community groups to determine what their perceptions are of the community's credit needs and whether national banks are helping to meet those needs.

This information helps provide examiners with the different points of view necessary to accurately assess a bank's level of compliance with fair lending laws.

It is very important to understand that making conclusive judgments on whether a bank is employing illegal discriminatory practice is, at best, a difficult task.

Illegal discrimination can occur in many subtle ways and rarely leaves tangible evidence in its wake. The Examiners fully explore any questionable policies or practices. Discussing these concerns with bank personnel and management is still the best way of making those individuals sensitive to these issues.

We believe we are experiencing increasing success with these communications.

With respect to prospective considerations, Chairman Dixon, we are reviewing several proposals to further promote compliance with fair lending laws. The proposals are at a very early stage of development.

No estimates of administrative costs, regulatory burden or supervisory benefits have yet been determined. We are continuing to study each of these alternatives, and others, to determine how they might improve our supervisory posture.

The proposals are, and I'll be brief:

An educational pamphlet for lenders, which really is a communication initiative; the sharing of community contact information among other regulators; and enhancement of the utilization of HMDA data, which has been spoken to by both Mr. Fiechter and Governor LaWare.

In conclusion, Mr. Chairman, I want to stress that the OCC is committed to enforcing fair lending laws and regulations. Our supervisory programs are efficient and effective in promoting compliance.

Our communication with the industry and bank customer groups has significantly heightened attention in all compliance areas.

We ensure compliance by requiring that corrective action is taken and violations will not recur.

We are aware that no system is perfect, but we are striving to make improvements in our processes.

I thank you.

[The complete prepared statement of Robert J. Herrmann follows:]

STATEMENT OF
ROBERT J. HERRMANN
SENIOR DEPUTY COMPTROLLER
FOR BANK SUPERVISION POLICY
OFFICE OF THE COMPTROLLER OF THE CURRENCY
Before the
SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE
October 24, 1989

Mr. Chairman, I am the Senior Deputy Comptroller for Bank Supervision Policy in the Office of the Comptroller of the Currency (OCC) and am responsible for formulating policies and procedures for the supervision of all national banks. In my testimony today, I will discuss how the OCC enforces fair lending laws and regulations, specifically in the context of illegal discrimination in mortgage lending.

The OCC's responsibilities for ensuring nondiscriminatory lending practices in national banks began in 1968 with passage of the Fair Housing Act. Over the past two decades, our responsibilities in this area have increased to also include enforcement of the Equal Credit Opportunity and Fair Credit Reporting acts, as well as the related legislation of the Community Reinvestment and Home Mortgage Disclosure acts.

The OCC's regulatory role and examination procedures primarily ensure that homebuyers who formally apply to national banks for mortgage credit are not treated discriminatorily on bases prohibited by law. Illegal discrimination in home finance can be particularly difficult to detect and measure because it can occur at so many different stages in the attempt to secure mortgage financing. Homebuyers may encounter illegal discriminatory behavior by sellers and their agents, by lenders, by appraisers, by insurers, or by advertisers -- all of whom may directly or indirectly affect financing of prospective purchases. Buyers may even "steer" themselves to lenders perceived as more receptive to their needs and away from lenders believed to be discriminatory.

Stated another way, potential customers can be affected by illegal discriminatory behavior at any one of four stages: during preliminary discussions with realtors, brokers, etc. on where to seek financing; when inquiring about mortgage loan terms with a bank's personnel; at the time of filing an application with a bank; or during the bank's credit decision process. Activities that occur prior to a bank's involvement are outside of our authority and ability to enforce as bank regulators. We can do little to detect illegal discriminatory behavior if it occurs prior to the bank's receiving a written application because there is no tangible evidence.

The Role of the OCC in Ensuring Compliance

The OCC's principal responsibility is to ensure that the national banking system operates safely and soundly. National bank assets represent over $1.8 trillion, or 60% of total assets of U.S. insured commercial banks, and we devote the majority of our resources to safety and soundness related supervision. However, we also devote significant resources to examinations designed to ensure that national banks comply with laws and regulations to which they are subject, including those prohibiting illegal discrimination in mortgage lending.

Three principles guide our efforts to promote compliance with fair lending laws and regulations. First, when illegal discrimination is found, both prospective and retrospective corrective action is required.

Second, conduct which adversely affects individuals protected by fair lending laws must be identified and eliminated.

Third, the OCC targets its resources to achieve the maximum benefit. The OCC's Compliance Program is an efficient and effective means of promoting compliance with laws and regulations throughout the national banking system.

Assessing Compliance

Under the Compliance Program, we annually examine institutions representing approximately 40 percent of national banking system assets. Examinations include an independent assessment of the level of compliance with fair lending laws. Examiners provide bank management and its board of directors not only a report of specific violations, but an assessment of the bank's own systems to detect and prevent problems. When examiners find problems that a bank's system did not detect, we require bank management to take corrective actions and we monitor the implementation of those actions.

To assess a bank's performance, examiners review bank policies, procedures, and underwriting standards. Examiners also evaluate a sample of loan applications to determine if a bank's decision to either grant or deny credit appears consistent with its stated policy. If discrepancies appear, especially on bases that cannot be used as criteria for loan decisions (e.g., race), examiners expand their review of application files to ensure that illegal discriminatory practices do not exist. A copy of the OCC's fair lending examination procedures are attached as Appendix A.

Tools used to enhance our fair lending examination process include Home Mortgage Disclosure Act (HMDA) data, Fair Housing Home Loan Data System analyses, and consumer complaint information.

The HMDA data are used to determine the distribution of home mortgage lending activity in a bank's community. This information helps in assessing a bank's role in meeting housing-related credit needs of the community. The OCC encourages each national bank to analyze the geographic distribution of all the loans it grants, particularly those involving housing-related credit. HMDA data facilitates this analysis. If a bank has not performed a HMDA data analysis or if a determination is made that the bank's analysis is inadequate, examiners perform the analysis. Geographic discrepancy in lending activity within a bank's service area is only an indicator of a bank's overall level of service to the community's credit needs. With the amendments to HMDA contained in the Financial Institutions Reform, Recovery and Enforcement Act of 1989, geographic analyses will provide a broader picture of the distribution of mortgage lending activity within applicable communities. However, HMDA data are insufficient to estimate or measure illegal discriminatory mortgage lending practices.

The Fair Housing Home Loan Data System (FHHLDS) was designed as an examination tool to assess whether mortgage lenders discriminate illegally. The system provides for the collection of mortgage loan application information necessary to perform statistical analyses of a bank's home loan decisions. These analyses identify whether or not statistical relationships exist between loan decisions and applicant characteristics (e.g., gender) that may indicate potential illegal discrimination in mortgage lending practices.

However, only a few national banks have sufficient home loan application volume to allow meaningful statistical analysis of a bank's fair lending performance. For example, the 1987 Compliance Program sample contained approximately 700 banks, of which only 272 had received more than 50 written mortgage applications in the previous twelve months. In order to perform analysis that might reveal patterns of adverse treatment of applicants, there must be a sufficient number of rejected applications. Of the 272 banks, only 24 had a sufficient volume of rejected applications to allow the performance of a valid FHHLDS analysis. None of the analyses performed indicated possible illegal discriminatory practices.

OCC's Consumer Complaint Information System might be an indicator of discrimination, but there have been very few discrimination related complaints filed with this agency. Of over 37,000 written complaints the OCC received between January 1987 and August 1989, only sixteen alleged racial discrimination in real estate lending. After investigating each of the complaints, no violations of law were cited. Copies of a small sample of these complaints, sanitized to protect the identity of the consumer and the bank, are attached as Appendix B for your information.

Correcting Violations

In order to promote uniform enforcement of the fair lending laws by the financial regulatory agencies, the OCC along with the Federal Reserve Board, the Federal Deposit Insurance Corporation and the National Credit Union Administration issued a "Joint Policy Statement for the Enforcement of the Equal Credit Opportunity and Fair Housing Acts" in 1981. This

Enforcement Policy Statement identifies the violations that are considered of such a serious nature that retrospective and prospective corrective action is required. They include:

- o Discouraging applicants on a prohibited basis;
- o Using credit criteria in a discriminatory manner in evaluating applications; and
- o Imposing different terms on a prohibited basis.

In addition to the Joint Policy Statement, the OCC issued a "Supplementary Enforcement Policy for the Equal Credit Opportunity and the Fair Housing Acts" and "Internal Guidelines -- Enforcement of the Equal Credit Opportunity and Fair Housing Acts" to provide national banks with further guidance by describing the specific actions that we will take in these egregious cases. Copies of these documents are attached as Appendix C.

Since April 1987, the OCC conducted 3,437 consumer compliance examinations. During these examinations, we cited 381 violations subject to the Policy Statement for the Enforcement of the Equal Credit Opportunity and Fair Housing acts in 239 banks. We did not find any violations of the Fair Housing Act or indications of illegal discrimination in real estate lending. The vast majority of these violations dealt with inadequate or incomplete adverse action notices. Regarding the violations cited, banks were required to conduct file searches for the previous 24 month period and correct both past and present violations. Bank management was required to revise policies and procedures to ensure that these violations would not recur.

The OCC does not rely solely on examinations to encourage banks to meet their fair lending obligations. Compliance with fair lending laws also includes an assessment of the bank's activities related to the Community Reinvestment Act (CRA). One of the assessment factors included in the CRA's implementing regulation requires examiners to review a bank's policies to determine if there are any underlying practices that are intended to discourage applications for types of credit offered by the bank. As appropriate, examiners conduct meetings with local community groups to determine what their perceptions are of the community's credit needs and whether national banks are helping to meet those needs. This information helps provide examiners with the balanced perspective necessary to accurately assess a bank's level of compliance with fair lending laws, rules and regulations.

It is very important to understand that making conclusive judgments on whether a bank is employing illegal discriminatory practices is, at best, a difficult task. Illegal discrimination can occur in many subtle ways and rarely leaves tangible evidence in its wake. Examiners fully explore any questionable policies or practices. Discussing these concerns with bank personnel and management is still the best way of making them sensitive to these issues.

There is one final dimension to the topic of discrimination which deserves treatment. The fundamental business of banking has undergone radical change in the last decade. Insured banks are no longer the sole providers of traditional bank products and services. A vast number of other competitors are now marketing loans at very competitive terms and rates. The evidence for this is all around us. This competition has forced banks to become more market and customer-oriented and the value of a customer has been immeasurably enhanced. These phenomena have focused successful banks on fitting services to customer needs. The result is that creditworthy customers at all economic stratas are being sought vigorously. Illegal discrimination simply does not make good business sense in this context.

Prospective Considerations

We are reviewing several proposals to further promote compliance with fair lending laws. The proposals are at a very early stage of development. No estimates of administrative costs, regulatory burden, or supervisory benefits have been determined. We are continuing to study each of these alternatives to determine how they might improve our supervisory process. The proposals are:

- o Educational pamphlet for lenders -- a pamphlet designed to increase lender awareness of practices, policies, and procedures that may be discriminatory;
- o Sharing community contact information -- establishing a system through which information gathered from community contacts by any financial regulatory agency would routinely be shared with all the other agencies; and
- o Enhanced utilization of HMDA data -- Providing revised aggregation reports for use in conducting analyses of geographic lending activities.

Conclusion

In conclusion, the OCC is committed to enforcing fair lending laws and regulations. Our supervisory programs are efficient and effective in promoting compliance. We ensure compliance by requiring that corrective action is taken and violations will not recur. We are aware that no system is perfect, but we are striving to make improvements in our processes. We will continue to analyze alternatives to improve our supervisory process of promoting compliance with antidiscrimination laws, rules and regulations.

Senator DIXON. Thank you, Mr. Herrmann.

There are several additional Senators who have arrived. We are delighted to see the distinguished Senator from Massachusetts, Senator Kerry, here.

Delighted to see the ranking member, the distinguished Senator from Missouri, Senator Bond.

And the distinguished assistant majority leader of the Senate, Senator Cranston, has another obligation in connection with the problems presently in his State and has asked to make a brief statement. We're delighted to have him here and delighted to hear that statement.

OPENING STATEMENT OF SENATOR CRANSTON

Senator CRANSTON. I thank you very much, Senator Dixon. I thank you for arranging this committee hearing, which is a very important one on a very important topic. And I thank other Senators for letting me make a brief statement at this point.

I have to go to do more work on the earthquake problem and that's why I will not be able to attend this hearing throughout its session, as I had wished to. And I'm sorry that I won't be able to hear the witnesses.

But we will have their record available and I look forward to reading that.

The problem of discrimination in mortgages is obviously a very disturbing circumstance. Its return to the national agenda, recent news accounts have concluded what many have suspected for a long time:

Racial, sexual and geographic mortgage discrimination continues to plague many, many Americans. This type of discrimination has to end.

All families deserve a decent place to live. Lenders play a vital role in providing decent homes. Lenders must be encouraged to provide Americans with a chance to own their own homes regardless of race or gender.

Many first-time home buyers face tremendous obstacles in purchasing homes these days. Prices are exorbitant. Interest rates are high. And starter homes are scarce.

Female-headed and minority families are further penalized by discriminatory activities. And all this is inexcusable.

Lenders must be encouraged to provide mortgages to all types of families. Lenders to reach out to minority and female-headed families as well as to struggling neighborhoods should be publicized and they should be rewarded.

Unfortunately, past mortgage discrimination statutes have provided few incentives for lenders to take a look at non-traditional home buyers. Information on lending patterns was not readily available. Penalties for engaging in discriminatory lending were negligible.

In the Thrift Reform package, we strengthened existing mortgage discrimination statutes. We provided for lenders to disclose to the public the racial income and gender of potential borrowers.

We provided for public disclosure of CRA ratings and evaluations. These changes are critical to address effectively racial, gender and geographic discrimination.

This hearing which Senator Dixon has arranged today is designed to make sure that the regulators who are charged with implementing these measures do so in a manner that is useful to the public.

I'm particularly interested in three issues that were contained in the conference report that accompanied the thrift reform bill. So I hope that the witnesses in the course of today will, first, describe the method used to collect and publicize the race, income and gender of potential/actual borrowers.

Second, defined the information to be classified as, quote, "Confidential Communication," between the lender and the regulator.

And, third, suggest any additional legislation that you believe is necessary to ensure an end to this type of mortgage discrimination.

Your help on those points and on other points will be deeply appreciated.

And, again, I thank you, Senator Dixon and all concerned for letting me interject myself at this point.

Senator DIXON. Well, we thank the distinguished Senior Senator from California.

May I say to my colleagues, if it's satisfactory, I'll complete the panel, may I say to my distinguished friend from Massachusetts and my friend from Missouri, before we recognize you for any further statement, unless you have a problem.

Thank you very much.

Mr. John Bovenzi, the Deputy to the Chairman of the FDIC. We're delighted to have you here, sir.

Mr. Bovenzi.

JOHN F. BOVENZI, DEPUTY TO THE CHAIRMAN, FEDERAL DEPOSIT INSURANCE CORPORATION, WASHINGTON, DC; ACCOMPANIED BY; JANICE SMITH, DIRECTOR, OFFICE OF CONSUMER AFFAIRS, FEDERAL DEPOSIT INSURANCE CORPORATION

Mr. BOVENZI. Thank you, Mr. Chairman, Senator Riegle, Senator Cranston, members of the subcommittee.

I am pleased to testify today on the Federal Deposit Insurance Corporation's report on loan discrimination. Our report concludes that most FDIC-supervised institutions are in satisfactory or better compliance with the Fair Lending laws.

However, we share this committee's concerns over recent studies which indicate possible disparities in mortgage lending. We will do whatever is necessary to address these concerns.

The FDIC enforces the various Fair Lending laws largely through its consumer compliance examination program. The Fair Lending examination procedures used by FDIC Examiners are being submitted for the record, as are the procedures for complaint investigations, including Fair Housing complaints.

These procedures are currently being revised to reflect changes made by FIRREA.

Evidence of an illegal discriminatory pattern or practice in mortgage lending is one of the most serious compliance violations for which an institution may be cited.

We have had to cite only five such violations during the last 3 years. Most Fair Housing violations generally are of a technical nature and, with few exceptions, once they are brought to an institution's attention, they are corrected.

In addition to compliance exams, CRA protests are an additional way to monitor possible illegal mortgage lending discrimination. Only one protest has been submitted to the FDIC during 1989.

Other useful indicators are the FDIC's toll-free hotline and written complaints and inquiries.

All of these indicators reinforce the findings of our examiners that most FDIC supervised institutions are in satisfactory or better compliance with fair lending laws.

A number of recent changes to the Fair Lending laws and procedures will enhance greatly the ability of both the public and the regulators to monitor compliance with and ensure the vigorous enforcement of the loan discrimination laws.

Most importantly, the Home Mortgage Act amendments in FIRREA will provide more specific data to make findings on discriminatory mortgage lending practices.

Even so, the FDIC is considering additional ways to enhance the monitoring and enforcement of anti-discrimination laws. We plan to strengthen our community outreach program. Currently, examiners make outside contacts during regular compliance examinations when necessary to assess an institution's performance.

However, the new program we plan to establish would provide for independent, nonexaminer community outreach specialists.

A new community affairs officer position would be established in our Office of Consumer Affairs as well as in each of our eight regional offices around the country.

These officers would be primarily responsible for meeting with consumer and community groups, government and industry organizations and others regarding community needs and the lending practices of institutions within their communities.

Senator DIXON. And have you done that, Mr. Bovenzi? You talk in the abstract. Have you done that?

Mr. BOVENZI. We've not set this program up to date. This is a program that we have just recently discussed with senior management and are planning to go forward with.

These community affairs officers would work independently of our compliance examiners. They would gather and analyze pertinent information regarding community credit needs and loan discrimination. They would provide the information and data to the examination staff to assist them in evaluating the Fair Lending performance of FDIC's supervised institutions.

The results also would be shared with other federal financial regulators.

That concludes my oral statement, Mr. Chairman, and I will be pleased to answer any questions.

[The complete prepared statement of John F. Bovenzi follows:]

TESTIMONY OF

L. WILLIAM SEIDMAN
CHAIRMAN
FEDERAL DEPOSIT INSURANCE CORPORATION
WASHINGTON, D.C.

ON

LOAN DISCRIMINATION

BEFORE THE

SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

10:00 A.M.
October 24, 1989
Room SD-538, Dirksen Senate Office Building

SUMMARY OF FDIC LOAN DISCRIMINATION TESTIMONY

As required by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA"), the FDIC recently submitted to the Congress a report containing findings on the extent of discriminatory lending practices by mortgage lenders subject to regulation or supervision by the FDIC.

Our report concludes that, fortunately, the great majority of FDIC-supervised institutions are in satisfactory or better compliance with the fair lending laws. Over the last three years, we have had only five citations against FDIC-supervised institutions for illegal discriminatory practices in mortgage lending.

The FDIC monitors possible illegal mortgage discrimination on the part of FDIC-supervised institutions primarily through our consumer compliance examinations. In recent years, we have steadily increased the number of these examinations we conduct each year. We also monitor such activity through CRA protests by the public against applications and through our toll-free consumer "hotline". Institutions that do not comply with consumer protection and civil rights laws and regulations find that violations can result in increased regulatory oversight, administrative actions, civil money penalties, and delays or denials of applications. No FDIC-supervised institution with a CRA rating of less than satisfactory has had an application approved without first agreeing to take appropriate corrective actions.

There have been a number of recent changes to the laws, regulations and procedures that relate to loan discrimination and fair lending compliance and enforcement. In FIRREA, Congress enacted several amendments to the Community Reinvestment Act and the Home Mortgage Disclosure Act. These changes, which become effective in 1990, will greatly enhance the ability of the public and the regulators to ensure compliance with and vigorous enforcement of the loan discrimination laws. In addition, the FDIC plans to establish a new program in the very near future in which independent community outreach specialists will be responsible for strengthening our efforts in the community outreach area. These individuals will provide information to the FDIC examination staff to assist them in evaluating the fair lending performance of FDIC-supervised institutions.

Finally, prior to enactment of FIRREA, the Federal Financial Institutions Examination Council Consumer Compliance Task Force had formulated ideas and possible recommendations for strengthening compliance with the fair lending laws. The FDIC does not want to advocate any of these ideas until we have had a chance to further analyze them in light of the recent changes in the fair lending enforcement area made by FIRREA.

Good morning, Mr. Chairman and members of the Subcommittee. We are pleased to testify today on the Federal Deposit Insurance Corporation's report on loan discrimination. This report was submitted to the Congress as required by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA"). Our report contained findings, based on a review of currently available loan acceptance and rejection statistics, on the extent of discriminatory lending practices by mortgage lenders subject to regulation or supervision by the FDIC.

Our report concludes that most FDIC-supervised institutions are in satisfactory or better compliance with the fair lending laws. However, we share the concerns of the Congress and the public regarding recent studies which indicate possible disparities in mortgage lending. We are committed to doing whatever is necessary to address these concerns.

The FDIC uses a number of legal tools to monitor and oversee the lending practices of FDIC-supervised institutions. These include the Fair Housing Act ("FHA"), the Equal Credit Opportunity Act ("ECOA"), the Community Reinvestment Act ("CRA"), and the Home Mortgage Disclosure Act ("HMDA").

The FDIC enforces these fair lending laws largely through its consumer compliance examination program. Despite a dramatic increase in the number of failed and problem institutions in recent years, which has required the FDIC to devote significantly more resources to problems involving safety and soundness, we have steadily increased the number of compliance examinations we conduct each year. In 1986, we conducted 1,228 compliance examinations; in 1987, 2,242; and in 1988, 3,066. For 1989, we expect approximately the same number of examinations as in 1988. More than 1,230 examinations were conducted during the first half of 1989. Our goal is to examine institutions rated 1, 2, or 3 for compliance once every 24 months, and institutions rated 4 and 5 at least every 12 months, with visitations conducted as necessary.

The FDIC provides its examination staff with a Manual of Compliance Examinations which contains explicit procedures to be followed in examining for compliance with the consumer protection and civil rights laws for which the FDIC has enforcement responsibility. These procedures are currently being revised to reflect changes in the laws made by FIRREA.

In evaluating an institution's compliance with consumer protection and civil rights laws, the FDIC uses two rating systems. One is the Consumer Compliance Rating System; the other is the Interagency CRA Assessment Rating System (See Attachment in FDIC Loan Discrimination Report). Under the latter, the CRA assessment factors contained in Part 345 of the

FDIC's Rules and Regulations are grouped into five "performance categories," including one category entitled "Discrimination or Other Illegal Credit Practices." It is in this performance category that we evaluate an institution's compliance with anti-discrimination and credit laws.

It is the FDIC's view that evidence of an illegal discriminatory pattern or practice in mortgage lending is one of the most serious compliance violations for which an institution may be cited. Over the last three years, FDIC-supervised institutions have been cited for only five such violations. Other fair housing violations we have found have generally been of a technical nature, primarily related to advertising, poster requirements and data collection.

Institutions that do not comply with consumer protection and civil rights laws and regulations find that violations can result in increased regulatory oversight, administrative actions, and civil money penalties. An institution also is likely to be subject to CRA protests and complaints, which can result not only in denials of applications, but in costly time delays. However, the FDIC's overall experience, with few exceptions, has been that once a problem is brought to an institution's attention, steps are taken to correct it. No FDIC-supervised institution with a CRA rating of less than satisfactory has had an application approved without first agreeing to take appropriate corrective actions.

The following table indicates the CRA ratings for FDIC-supervised institutions examined during the past three years:

CRA Ratings

Year:	1	2	3	4 and 5
1986	115	1,086	19	1
1987	221	1,965	40	8
1988	307	2,683	58	12

Our composite consumer compliance ratings are an additional measure of possible discriminatory patterns and practices. The following table indicates the composite compliance ratings for FDIC-supervised institutions during the past three years:

Composite Compliance Ratings

Year	1	2	3	4 and 5
1986	178	891	148	11
1987	319	1,617	290	16
1988	472	2,166	394	34

Based on CRA and composite compliance ratings, it can be seen that, fortunately, the great majority of FDIC-supervised institutions are in satisfactory or better compliance with the fair lending laws.

CRA protests by the public against applications provide the FDIC with an additional vehicle through which we can monitor possible illegal mortgage lending discrimination by FDIC-supervised institutions. The FDIC received two CRA-related application protests in 1986 (against two institutions), nine in 1987 (against seven institutions) and five in 1988 (against five institutions). One protest has been submitted during 1989.

The FDIC's toll-free "hotline" is another useful indicator of possible lending discrimination practices. During 1988, the FDIC's Office of Consumer Affairs and our Regional Offices reported approximately 39,400 telephone calls for information and assistance. Of this number, 331 calls involved community reinvestment matters and 711 involved fair housing. For the first eight months of 1989, nearly 32,200 telephone calls were reported, with 348 relating to community reinvestment and 1,190 concerning fair housing matters. Many of these calls were from bankers in connection with regulation revisions. In 1988, OCA and the Regional Offices also received about 3,500 written complaints and inquiries, twenty of which involved CRA-related issues and three of which involved fair housing. During the first eight months of 1989, over 2,900 written complaints and inquiries were received. Six of these involved community reinvestment and four involved fair housing. We made no findings of mortgage lending discrimination in any of these instances.

The FDIC encourages the public to advise us of possible noncompliance by FDIC-supervised institutions with the laws the FDIC is charged with enforcing. The FDIC reviews, responds to and follows-up on all complaints received. If we receive a complaint concerning mortgage redlining, we usually perform an on-site investigation at the affected institution. All allegations of substantive, as well as technical, violations of law are taken seriously.

RECOMMENDATIONS

There have been a number of recent changes to the laws, regulations and procedures that relate to loan discrimination and fair lending compliance and enforcement. Some have been statutory changes -- others have been instituted by the agencies of their own volition. For example, the federal financial institution supervisory agencies issued a revised CRA policy statement in March, 1989 for the specific purpose of strengthening the agencies' oversight and enforcement of CRA.

The recent amendments to CRA and HMDA contained in FIRREA provide for significant new authorities and data that will enhance greatly the ability of both the public and the regulators to monitor compliance with, and ensure the vigorous enforcement of, the loan discrimination laws. Most importantly, once the amendments to HMDA become effective and the information required by those amendments becomes available, the agencies and the public will have at their disposal more specific data to make findings on discriminatory mortgage lending practices such as those requested by the Loan Discrimination Report in FIRREA.

Beginning in 1990, HMDA will require disclosure by financial institutions of both (1) data on loan applications and their disposition and (2) the race, sex and income of borrowers and applicants. The Federal Reserve Board, in consultation with the other agencies, recently published proposed revisions to Regulation C implementing these new requirements. These revisions would require a "register" form of reporting under which lenders would record the required data on a loan-by-loan and application-by-application basis. These registers would be submitted to the federal supervisory agencies and reports reflecting individual institution and aggregate data will be generated. Thus, the information that will be available in the future as a result of these changes to the law should go a long way in addressing the need for changes to assure nondiscriminatory lending practices.

Even so, the FDIC has given significant consideration to additional ways in which we can further enhance the monitoring and enforcement of anti-discrimination laws. As a result, we anticipate the establishment of a new program in the very near future that will strengthen our efforts in the area of community outreach. FDIC policy currently provides that examiners should make outside contacts during regular compliance examinations when necessary to assess an institution's performance in meeting community credit needs. In addition, the FDIC's outreach efforts include representation at meetings, conferences and seminars sponsored by the FDIC and by community and industry groups.

However, the new program we plan to establish would provide for independent, community outreach specialists. A new position, Community Affairs Officer, would be established under our Office of Consumer Affairs, which is an independent office reporting directly to the Office of the Chairman. A similar position also would be created for each of our eight Regional Offices, reporting to the Office of Consumer Affairs. These Officers would be primarily responsible for making contact and meeting with consumer and community groups, government and industry organizations, and others regarding community needs and the lending practices of institutions within their communities. These individuals would work independently of our compliance examiners and thus would be supplementing their analysis. However, they would provide information and data to the examination staff to assist them in evaluating FDIC-supervised institutions as to their fair lending performance. The results of these efforts to gather and analyze pertinent information regarding community credit needs and loan discrimination also would be shared with other federal financial regulators.

Finally, prior to the enactment of FIRREA, the Federal Financial Institutions Examination Council Consumer Compliance Task Force had formulated ideas and possible recommendations for strengthening compliance with the fair lending laws. The FDIC does not at this time want to advocate any of these ideas until it has had a chance to analyze the need for such measures in view of the fair lending enforcement enhancements contained in FIRREA. Further, at this time the concepts have not been reviewed by the Council, but are only ideas formulated by the Task Force.

Fair Lending examination procedures used by FDIC Examiners

EQUAL CREDIT OPPORTUNITY

INTRODUCTION

The Equal Credit Opportunity Act (ECOA)(15 U.S.C. 1691) became effective on October 28, 1975 and is implemented by Federal Reserve Board Regulation B. The ECOA was amended on March 23, 1976 and the revised Regulation B was effective on March 23, 1977. Regulation B was revised again on December 16, 1985 with mandatory compliance effective on October 1, 1986. An official staff commentary providing interpretive guidance was also added at that time.

Regulation B prohibits discrimination in any aspect of a credit transaction on the basis of race, color, religion, national origin, sex, marital status, age (provided that the applicant has the capacity to enter into a binding contract), receipt of income from a public assistance program, and the good faith exercise of any right under the Consumer Credit Protection Act.(202.4) These factors are referred to throughout the regulation and this section as "prohibited bases."(202.2(z)) In addition, it is unlawful to discriminate against an applicant because of the race, color, religion, national origin, sex, marital status or age of the applicant's business associates or of the persons who will be related to the extension of credit (e.g., those residing in the neighborhood where the collateral is located).

Illegal discrimination means treating an applicant or group of applicants less favorably than another individual or group on a prohibited basis.(202.2(n)) Regulation B sets forth certain acts and practices which are specifically prohibited or permitted. To limit discrimination, it imposes a balance between a bank's need to know about a prospective borrower and the borrower's right not to disclose information irrelevant to the transaction.

The regulation deals with taking, evaluating and acting on applications for credit accounts and the furnishing and maintenance of credit information. It does not prevent a creditor from obtaining information necessary to evaluate the creditworthiness of an applicant.

DEFINITION OF CREDITOR

All creditors are subject to Regulation B, which defines a creditor as follows:

- A person who regularly participates in the decision of whether or not to extend credit.
- A creditor's assignee, transferee, or subrogee who participates with the creditor in the credit decision.
- A person who regularly refers applicants or prospective applicants to creditors or selects or offers to select creditors to whom requests for credit may be made. Such persons (e.g., automobile dealers, home improvement contractors, real estate brokers, etc.) are only subject to sections 202.4 and 202.5(a) which make discrimination on a prohibited basis illegal generally and in particular by discouraging applications on a prohibited basis. If a violation of the ECOA or Regulation B is committed by a creditor, another creditor is not liable for the violation unless it knew or had reasonable notice of the act, policy or practice that constituted the violation.

The term "creditor" does not include a person whose only participation in a credit transaction involves the honoring of a credit card.(202.2(l))

TAKING THE APPLICATION

Discouraging Applications

Regulation B's concern with the application process starts before the application is taken. Lending officers and employees must be aware of the provisions of the regulation and must take no action that would, on a prohibited basis, discourage a reasonable person from applying for a loan. This prohibition applies to oral and telephone inquiries, personal contract and advertising.

Regulation B does not distinguish between oral and written applications in its prohibition of discriminatory action. Therefore, in the interview prior to and during the taking of an application, lending officers must refrain from asking for prohibited information. Questions must be neutral with regard to sex and asked of all applicants who desire the same type and amount of credit.(202.5(a))

Inquiries Concerning Marital Status

Individual Credit — Generally, when an applicant applies for individual credit, the bank may not ask the applicant's marital status. There are two exceptions to this rule. The bank may ask the applicant's marital status:

- If the credit transaction is to be secured. (This information may be necessary to determine access to the collateral in the event of default.)
- If the applicant resides in a community property state, or lists assets located in such a state to support the debt. (In community property states, assets owned by a married person may also be owned by the spouse, thus complicating access to the asset in the event of default.) The examiner should determine whether such laws exist in the state in which a particular bank extends credit.(202.5(d)(1))

Joint Credit — Whenever a request for credit is joint (made by two or more persons who will be primarily liable), the bank may ask the applicants' marital status regardless of whether the credit is to be secured or unsecured.

Terminology — If the bank is permitted to request marital status, only the terms "married," "unmarried" and "separated" may be used. This pertains to both oral and written requests. "Unmarried" may be defined to include divorced, widowed or single, but the application must not be structured in such a way as to encourage the applicant to distinguish among these categories. The bank may ask questions which could indirectly disclose marital status to obtain relevant information. These questions may concern the source of income or ownership of assets supporting the debt and whether the debt obligations of the applicant have a co-obligor. However, any such question must not be structured so as to force the applicant to indicate marital status. A bank may inquire whether the applicant is obligated to make alimony, child support or separate maintenance payments to determine the applicant's total obligations.(202.5(d)(1))

Request for Information Concerning Spouse or Former Spouse

The bank must not inquire about the applicant's spouse or former spouse either on the application or orally, unless one of the following conditions exists:

- The spouse will be a user of, or contractually liable on, the account.
- The applicant is relying on a spouse's income to repay the debt.
- The applicant resides in or is relying on property located in a community property state to support the credit request.
- The applicant is relying on alimony, child support or separate maintenance income to repay the debt.

In general, when a bank uses an application form for more than one purpose, the application must contain a disclosure that information about the applicant's spouse is not required unless one of the above conditions exists.(202.5(c))

Alimony, Child Support and Separate Maintenance Income

Income derived from alimony, child support or separate maintenance payments need not be revealed unless the applicant wishes to rely on it to repay the debt. The applicant must be advised of that option before any questions concerning such payments are asked. The advice also must precede, on any printed application, any general request concerning income and the source of income. Therefore, a creditor must either ask questions designed to solicit only such specific information about income as salary, wages, employment income, or must state that disclosure of alimony, child support, or separate maintenance payments is not required. However, the bank may inquire about the liability of an applicant to make such payments.(202.5(d)(2))

Childbearing Intentions or Capability

The bank may never request information about an applicant's birth control practices or childbearing intentions or capability. The bank may inquire about the continued ability to repay the debt, such as the probability of continued employment. However, the request must be made of all applicants who are similarly qualified without regard to any prohibited basis. The number, ages and expenses of present dependents may also be requested.(202.5(d)(4)).

Other Prohibited and Permitted Requests

Regulation B specifically prohibits banks from inquiring about an applicant's sex. Written applications must contain only terms which are neutral with regard to sex. For example, in the past, many applications contained terms "husband" and "wife." Courtesy titles which indicate sex, i.e., Mr., Mrs., Ms., Miss, maybe requested, but only if accompanied by a conspicuous statement that the designation of any such title is optional.(202.5(d)(3))

The regulation also prohibits inquiry about an applicant's race, color, religion or national origin. An exception exists when the bank extends home loans. Part 338 of the Corporation's Rules and Regulations requires the bank to note race/national origin and sex when taking an application for a home loan. The applicant's age and marital status must also be noted. The bank may inquire about an applicant's permanent residence and immigration status to determine creditworthiness but not to deny credit on the grounds of national origin.(202.5(d)(5))

The regulation permits a bank to request a list of all accounts upon which the applicant is liable, the name and address in which the accounts are carried, and any other names used previously to obtain credit.(202.5(c)(3))

Sample application forms have been included in Regulation B for the following types of credit: open-end and unsecured credit, closed-end and secured credit, closed-end and either secured or unsecured credit, residential real estate credit, and credit extended in community property states. The regulation does not require that banks use written applications. However, if a bank desires to use them, either the appropriate model application form in Appendix B of the regulation, or one which otherwise complies, must be employed. The model form may be modified by asking for additional nonprohibited information, by excluding any information not desired, or by changing the format provided the required disclosures are made.

EVALUATING THE APPLICATION

Judgemental and Credit Scoring Systems

A bank may evaluate creditworthiness by using either a judgmental system, a demonstrably and statistically sound, empirically derived, credit scoring system or a combination of both systems.(202.6)

A demonstrably and statistically sound, empirically derived, credit scoring system is a system which has the capability of differentiating between creditworthy and noncreditworthy applicants with statistically significant probability. Values, or scores, are assigned to credit applicants in direct proportion to the predictive value of variables employed in the scoring system. The requirement that a scoring system be "demonstrably sound" means that a clear relationship must be shown between the measure of creditworthiness and the set of predictive variables used in the scoring system. Initially, a bank may adopt a scoring system developed from a source not directly related to the bank's own credit experience. However, once a bank has adopted a scoring system, it must be "validated" periodically. Validation is a process by which the bank demonstrates that the variables used in its scoring system are, or continue to be, predictive of the creditworthiness of applicants. Once sufficient credit experience under a scoring system has been gained, a bank must use the observed creditworthiness of its own customers to test whether the system is "valid" (i.e., predictive at statistically significant levels). Any time a validity test is performed and either the set of scoring variables are found nonpredictive or the scores being used are found to be inappropriate (i.e., nonproportional to their predictive value), the scoring system is no longer "demonstrably and statistically sound, empirically derived" and it is invalid.(202.2(p))

A judgmental system is any system, other than a credit scoring system, used to evaluate creditworthiness. As a general rule, most banks have guidelines for evaluating credit requests which are often based on the same predictive factors used in credit scoring systems. However, values are not assigned to the factors and the system is not statistically valid. Loan officers judgmentally evaluate the application, then accept or reject the credit request.(202.2(t))

Some banks use a combination of the two systems to evaluate credit. An application is scored using a credit scoring system. If the results are close to the accept/reject cutoff, the bank may use a judgmental override. Loan officers review the scored application and judgmentally render the credit decision.

Neither judgmental nor credit scoring evaluation systems can discriminate among applicants using prohibited bases as variables in the credit evaluation process. Examples of factors which cannot be used in evaluating credit or may only be used provided certain conditions are met are as follows:

- Childbearing Practices — Regulation B absolutely prohibits those credit evaluation policies which consider the applicant's probability or capability of bearing or rearing children. Also, a bank may not consider the likelihood that the applicant's income will be interrupted by childbearing or question the applicant about such intentions. However, the bank is permitted to consider the number and ages of the applicant's dependents and any related expenditures.(292.6(b)(3))

- Telephone Listing — A bank may not consider whether there is a telephone listing in the name of the applicant, although it may consider whether or not there is a telephone in the applicant's residence.(202.6(b)(4))

- Age — In a demonstrably and statistically sound, empirically derived credit scoring system, the age of an elderly applicant cannot be assigned a negative score.(202.6(b)(2)(ii)) In a judgmental system of evaluating creditworthiness:

  —Age may be considered to determine if the applicant has the capacity to enter into a binding contract.

  —Age of an elderly applicant may always be considered when used in the applicant's favor.

  —Age may be used in connection with occupation to determine the amount of employment income and/or retirement income which will support the debt until maturity.

  —Age may be considered in assessing the adequacy of any security offered if the duration of the loan exceeds the applicant's life expectancy.

  —Age may be considered to assess the significance of the applicant's length of employment or residence.(202.6(b)(2)(iii))

- Income — The bank may not discount the income of an applicant or spouse on a prohibited basis or because it is part-time. The income of a spouse used in a joint application for credit must be considered equally with a that of the applicant. In addition, income derived from annuity, pension or retirement benefits must not be discounted. The bank may, however, consider the amount and probable continuity of any income and must consider alimony, child support or separate maintenance income if disclosed by the applicant to the extent that those payments will be continuing.

Factors considered in determining the likelihood of continuing payments may include, but are not limited to:

—Whether the payments were provided for by oral or written agreement or by court decree.

—The length of time payments have been made.

—Whether the receipt of payments has been recent and regular.

- —The ability to compel payment.
- —The creditworthiness and credit history of the payor when available to the bank in accordance with the Fair Credit Reporting Act or other law.(202.6(b)(5))

Additional considerations exist when a bank judgmentally evaluates income from a public assistance program, such as:

- —The length of time the applicant has been receiving income derived from a public assistance program.
- —Whether the applicant will continue to meet residency requirements for public assistance benefits.
- —The status of dependents to ascertain the continuity of benefits received relating to such dependents.(202.6(b)(2)(iii))

Credit History

If a bank considers credit history in evaluating applications, then all accounts for which the applicant was or is a user or contractually liable should be considered, even those that are not listed in the applicant's name.(202.6(b)(6)) At the applicant's request, the credit history must include any account reported in the name of the applicant's spouse or former spouse which accurately reflects the applicant's ability or willingness to repay. At the request of the applicant, the bank must also consider any information the applicant presents indicating that the credit history does not accurately reflect ability or willingness to repay.(202.6(b)(6)(ii) and (iii))

Other Considerations

The bank may consider the applicant's marital status, source of income, and permanent U.S. residency or immigration status to ascertain the bank's rights and remedies with respect to payment.(202.6(b)(7))

The Effects Test

In addition to the preceding rules for evaluating applications, all credit practices are subject to the "effects test." Effects test practices, while not discriminatory in intent, have a disproportionate adverse impact on protected class members (those persons covered by one of the prohibited bases).(202.2(z)) Under the effects test, a bank may be in violation of the ECOA if a particular practice has a disproportionate adverse impact on a protected group and is not reasonably related to creditworthiness. For example, a requirement that applicants have unreasonably extensive credit histories in order to receive credit may be illegal discrimination because of its disproportionate adverse effect upon married women.(202.6(a))

ACTING ON THE APPLICATION

Offering Accounts

A bank must not refuse, on the basis of sex, marital status, or any other prohibited basis, to grant and individual account to a creditworthy applicant. Any state law prohibiting separate accounts to married persons is pre-empted by the regulation, including laws which combine separate accounts for purposes of determining finance charges or loan ceilings. If the bank offers joint liability on accounts to married couples, it must also offer such accounts to unmarried persons.(202.7(a) and 202.11(b)(1)(ii) and (c))

The bank must not refuse to allow an applicant to open or maintain an account in a birth given first name, a birth given surname, spouse's surname or combined surname. For example, Mary Smith who is married to John Jones, may open an account in any of five different names: Mary Smith, Mary Jones, Mary Smith-Jones, Mary Jones-Smith or Mrs. John Jones. However, the bank may require that the applicant use one name consistently in doing business with the bank. In addition, the bank may inquire whether the applicant has obtained credit in another name, or is liable for accounts listed in another name, to determine the applicant's credit history.(202.7(b))

Actions on Existing Open-End Accounts

A bank may not require a reapplication, change the terms of an existing open-end account or terminate the account on the basis of age or retirement or because of a change in the applicant's name or marital status unless there is evidence of inability or unwillingness to repay. A denial of liability on the account by any account holder may be determined to be an unfavorable change in creditworthiness because of unwillingness to repay. For example, upon divorce, one of the applicants may deny further liability on the account. When the account is based on one spouse's income, and the other spouse's income at the time of the credit extension would not support the credit, the bank may require a reapplication upon a change in the applicant's marital status.(202.7(c)(1))

Signature Requirements

A bank's right to require signatures on credit instruments is limited by the regulation. The bank must also consider how property is held and state property laws in determining what credit instruments need to be signed to ensure repayment of the debt. Blanket policies of automatically requiring certain individuals (such as spouses) to sign the notes are prohibited. Banks must evaluate each credit request separately, determine how property used as collateral or support for the debt is held, and what signatures are necessary on which credit instruments to perfect a valid lien and ensure repayment of the debt. The bank's reasons for obtaining signatures should be clearly documented in the file as evidence of compliance with the regulation.(202.7(d))

If an applicant qualified individually for credit under the bank's standards of creditworthiness for the amount and terms requested, the bank may only require the signature of the applicant. If a joint applicant is volunteered, the signature of the joint applicant may also be required on any necessary credit instrument.(202.7(d)(1))

Other signatures may be required in the following circumstances:

- If the credit is to be unsecured and the bank is looking to the applicant's property as support for creditworthiness, the bank may consider the effect of state law, how the property is owned and other factors that may affect the value to the bank of the applicant's interest in the property. If the applicant's interest in the property is insufficient to establish creditworthiness, the bank may require the spouse or other joint owner to sign any instrument necessary or reasonably believed to be necessary, under applicable state law, to allow the bank to gain control of sufficient property to satisfy the debt in the event of default.(202.7(d)(2))
- If the credit is to be unsecured and the applicant is married and resides in a community property state, or the property supporting the debt is located in such a state, the bank may require the spouse's signature on those instruments necessary, or reasonably believed to be necessary, to make the community property available to the bank in the event of default. The bank may not require the spouse's signature if the applicant can manage or control sufficient community property to establish creditworthiness or if the applicant has sufficient separate property to qualify without utilizing community property.(202.7(d)(3))
- If the credit is to be secured, the bank may require the signature of the applicant's spouse or a joint owner of assets on any instrument necessary, or reasonably believed to be necessary under applicable state law to allow the bank to gain control of the applicant's interest in the assets in the event of default. Those instruments may include any instrument necessary to create a valid lien, pass clear title, waive inchoate rights or assign earnings.(202.7(d)(4))
- If the entire value of an asset is needed for an applicant to qualify for secured credit, the bank may require the signature of the applicant's spouse or other joint owner of the asset on any instrument necessary to make the asset available to satisfy the debt in the event of default. Or, if the debt is secured by real property and state law requires that all owners sign the mortgage to create a valid lien, the bank may require the signature of a spouse or other joint owner on the mortgage.

The bank may always request a cosigner or guarantor on an extension of credit if the applicant does not meet the bank's creditworthiness standard for individual credit. The request must not be made as a result of discrimination on a prohibited basis and must be required of all similarly qualified applicants applying for the same type and amount of credit. Whenever a cosigner or guarantor is requested, the choice of such a second party must be left to the applicant. The bank may not require that it be the applicant's spouse. The bank must evaluate the creditworthiness of both the applicant and the additional party in deciding to grant or deny the credit request.(202.7(d)(5))

Effective October 1, 1986, the definition of "applicant" was expanded to include guarantors, sureties, endorsers and similar parties. This provides legal recourse under section 706 of ECOA for parties, particularly spouses, who are required to become contractually liable in one of the aforementioned capacities on a prohibited basis.

Insurance

When the bank offers casualty, credit life, health, accident or disability insurance in connection with extending credit, differences in cost, terms or availability of the insurance will not constitute violations of the regulation. However, the bank may not deny or terminate credit merely because such insurance is unavailable on the basis of the applicant's age. When insurance is involved in the application, information regarding the applicant's age, sex or marital status may be requested solely to determine eligibility for the insurance.(202.7(e))

NOTIFICATION

Notification of Action Taken

The bank must notify the applicant of action taken on an application within 30 days after receipt of the completed written or oral application. Notification of both favorable and adverse action is required.(202.9(a)(1)) If the bank and the applicant agree that the applicant will inquire about what action was taken, the bank may consider the application withdrawn if the bank approves it and the applicant fails within 30 days to inquire about the action taken. In that case, no notification is required.(202.9(e)) Notification requirements for favorable action may be satisfied by receipt by the applicant of a coupon book, credit card, etc.(202.9(a)(1))

Notification of Adverse Action

For purposes of providing notification of action taken, preparing a statement of reasons for denial and retaining records, adverse action may be defined as:

- Refusal to grant credit in substantially the amount or on substantially the terms requested, unless an alternative offer is accepted by the applicant.
- Termination of an account or adverse change in terms, if the same action is not taken on a substantial portion of similar accounts.
- Denial of an increase in the credit extension when requested according to procedures established by the bank for the type of credit involved.(202.2(c)(1))

Adverse action excludes:

- Any change in the terms of an account which is expressly agreed to by the applicant.
- Any action or inaction resulting from inactivity, delinquency or default on the account.
- A refusal or failure to authorize an account transaction or loan at a point of sale which affects a substantial portion of similar accounts.(202.2(c)(2))

Any adverse action, such as a counter offer, taken on a prohibited basis is a violation of the ECOA.

Notice of adverse action taken on an uncompleted application or on an existing account must be given within 30 days after the action is taken. An uncompleted application is one for which the bank has not received all the information which it regularly obtains and considers for the type and amount of credit requested. The bank must attempt to obtain missing information and allow the applicant to complete the application.(209.9(a)(1))

Effective October 1, 1986, creditors must handle incomplete applications in one of the following ways within 30 days of receiving such an application:

- Provide notification of approval or adverse action, as appropriate.
- Request in writing the information needed to complete the application, designate a reasonable period of time for the applicant to furnish it and inform the applicant that if the information is not provided no further consideration will be given the application. Only if the applicant furnishes the requested information is the creditor required to notify the applicant of action taken.(202.9(c))

When the bank offers credit to the applicant other than in substantially the amount or on substantially the terms requested by the applicant, the bank must notify the applicant of the adverse action within 90 days if the applicant has not accepted the terms during that time.(202.9(a)(1))

Whenever adverse action is taken, the bank must furnish the applicant with:

- A written statement of the action taken.(202.9(a)(2))
- A written statement substantially similar to the following: "The Federal Equal Credit Opportunity Act prohibits creditors from discriminating against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age (provided that the applicant has the capacity to enter into a binding contract), because all or part of the applicant's income derives from any public assistance program or because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. The federal agency that administers compliance with this law concerning this bank is the Federal Deposit Insurance Corporation (Region identification and Regional Office address)."(202.9(b)(1))
- A written statement of the specific reasons for the action taken or disclosure of the applicant's right to such a statement within 30 days after the bank receives a request and that the applicant must make any such request within 60 days of the notice of action taken. The disclosure must include the name, address and telephone number of the person from whom or office from which the reasons may be obtained. When the bank chooses to disclose orally the reasons for denial, the applicant must also be informed of the right to receive written confirmation of those reasons within 30 days after receipt of a written request for confirmation.(202.9(a)(2)(i) and (ii))

When the bank discloses the specific reasons for adverse action, the bank may:

- Formulate a checklist or letter providing the specific principal reasons for adverse action; or
- Use all or a portion of the sample form in Appendix C to the regulation in order to comply with both Regulation B and the Fair Credit Reporting Act.

In the case of two or more applicants, the notification of action taken need only be given to the primary applicant where one is readily apparent.(202.9(f))

When more than one creditor is involved in a transaction and the applicant expressly accepts or uses credit offered by one of them, no notification need be delivered. However, if all deny credit or any counter offer is not accepted, each creditor must make the required notification. The notification may be provided by a creditor or indirectly through a third party if the identity of all creditors taking the action is given. The bank must see to it that all information is given accurately and in a timely manner to the party providing the notification.(202.9(g))

A bank may meet the requirements of notification by delivering or mailing a written notice to the applicant's last known address, or orally if the bank received 150 applications or less during the preceding calendar year.(202.9)

FURNISHING CREDIT INFORMATION

A bank is not required to report credit information on accounts. If the bank does so, however, certain requirements of the regulation become applicable. In particular, the bank must determine whether an account may be used by the applicant's spouse or whether both applicant and spouse will be contractually liable. Contractual liability in this case would not include secondary parties to the account, such as endorsers or guarantors. Any history of an account shared by the applicant and spouse, either as user or contractually liable party, must be designated to reflect the participation of both spouses. However, the bank need not change the name in which the account is carried or designate whether a spouse is a user or is contractually liable.(202.10(a))

Any shared account designated to reflect the participation of both spouses must be treated as joint for reporting purposes.(202.10(a)) The bank must furnish general credit information to a consumer reporting agency in a manner that will enable the agency to locate information on the account in the name of each spouse. When a bank is asked to furnish credit information on a specific person, it must provide that information in the name of the spouse about whom such information was requested.(202.10(c)) Inadvertent errors resulting in failure to comply with requirements of furnishing credit information will not be violations of the regulation if the bank takes corrective action and begins complying immediately upon discovery of the error.(202.14(c))

RETENTION OF RECORDS

All Accounts

The bank must retain the original or a copy of the following information for 25 months after the date it notified the applicant of action taken on the application:

- Any application, information required to monitor compliance with the ECOA, and all written or recorded information used in evaluating the application which has not been returned pursuant to the applicant's request.
- A copy of written documents and any recorded notation of oral notification of action taken on the application, the statement of specific reasons for adverse action and any written statement from the applicant alleging a violation of the regulation or the ECOA.(202.12(b)(1))

Accounts on Which Adverse Action Has Been Taken

The bank must also retain the original or a copy of the following information for 25 months after the bank informs the applicant of adverse action regarding an existing account:

- Any written or recorded information concerning such adverse action.
- Any written statement from the applicant alleging a violation of Regulation B or the ECOA.(202.12(b)(-2))
- Effective October 1, 1986, any written or recorded information on withdrawn or incomplete applications.(202.12(b)(3))

If the bank has been notified that it is under investigation for any violation of the regulation, it must retain all the above required information until final disposition of the matter.(202.12(b))

Inadvertent Errors

Inadvertent errors in record retention are not violations of the regulation. Prohibited information found in the bank's files is also not a violation if obtained prior to March 23, 1977 (or June 30, 1976 for sex and marital status information) or at any time from a consumer reporting agency, or when voluntarily given without request from the bank. Neither is it a violation to obtain information required by the appropriate enforcement agency to monitor compliance. Although the bank may retain such information in its files, it must not be used to evaluate creditworthiness.(202.12 and 202.14(c))

SPECIAL PURPOSE CREDIT PROGRAMS

The following types of credit programs meet the definition of special purpose credit programs:

- Any credit assistance program authorized by federal or state law for economically disadvantaged persons.(202.8(a)(1))
- Any credit assistance program offered by a nonprofit organization for its members or for economically disadvantaged persons.(202.8(a)(2))
- Any special purpose credit program offered by a profit-making organization to meet special social needs. Such a program must meet the following requirements:
  - —A written plan must be developed which designates eligible applicants and the procedures and standards for the extension of credit.
  - —The program will extend credit to those applicants who probably would not be able to obtain such credit on substantially similar terms as other applicants.(202.8(a)(3))

If the applicants in special purpose credit programs are required to have one or more common characteristics, such as race, color, religion, national origin, sex, marital status, age or receipt of income from a public assistance program, the bank may request and consider those characteristics in determining the eligibility of applicants.(202.8(c)) If financial need is to be used to determine eligibility, information concerning the applicant's marital status, income from alimony, child support, or separate maintenance payments, and financial information on the spouse may be requested and considered.(202.8(d)) In addition, the signature of the spouse or other person on the application or credit instrument may be obtained if required by federal or state law and will not be considered a violation of the regulation.(202.8(d))

Any denial of credit to any applicant who does not qualify for a special purpose credit program is not considered a violation of the regulation so long as the program is not established or administered on an illegal, discriminatory basis.(202.8(a))

INFORMATION FOR MONITORING

Credit Secured by Residential Real Property

To monitor compliance with the regulation, a bank must request and maintain the following information regarding written applications for credit relating to the purchase of, and secured by, residential real property (residential real property means improved real property, including one-to-four family dwellings and individual units of condominiums and cooperatives used for residential purposes):

- Race/national origin, using these categories: American Indian or Alaskan Native, Asian or Pacific Islander, Black, White, Hispanic, Other (Specify).
- Sex.
- Marital status, using the categories: Married, Unmarried and Separated.
- Age.(202.13(a))

The information may be requested on the application form or on a separate sheet of paper referring to the application. The applicant and joint applicant must be informed that the disclosure of such information is optional and that the information is being requested by the federal government to monitor compliance with federal laws prohibiting discrimination on the basis of race/national origin, sex, marital status and age. Refusal by the applicant to supply the requested information must be noted on the form containing the request.(202.13(b) and (c))

Effective October 1, 1986, monitoring information must be requested on applications for credit primarily for the purchase or refinancing of the applicant's principal residence, where that dwelling will secure the extension of credit. Dwelling is defined as a residentail structure that contains one-to-four units, whether or not that structure is attached to real property. This would include an individual condominium or cooperative unit, and a mobile or other manufactured home.

The monitoring provisions of Part 338 of the Corporation's Rules and Regulations constitute a substitute program adopted under section 202.13(d) of Regulation B. Consequently, a bank collecting data and making appropriate disclosures in compliance with Part 338 need not comply with the monitoring requirements of section 202.13(a), (b) and (c).

SPECIALIZED CREDIT

Dealer Paper

When a bank purchases indirect paper from a dealer in the regular course of business and it participates in the decision to extend credit, the bank must maintain procedures to determine whether the dealer is complying with the ECOA in all aspects of the credit transaction.(202.2(l))

If within 30 days the applicant accepts a credit offer from the bank, no further notification is required from either the bank or the dealer. If credit is not extended by the bank or the applicant does not accept the bank's offer of alternate terms, each creditor taking adverse action must notify the applicant. For example, if a dealer attempts unsuccessfully to obtain financing at several banks or the applicant does not accept any alternate terms offered, all the banks and any dealer acting as a creditor in the transaction must give the notices required for adverse action. A bank may enter into contractual arrangements with dealers to provide all appropriate notices. If the dealer provides a joint notification, the bank will not be liable for actions or omissions resulting in violations if it provided the dealer with the information necessary to comply with the notification requirements and was maintaining procedures reasonably adapted to avoid any such violation. Any joint notification must identify each creditor.(202.9)

All creditors involved in an indirect credit transaction must retain all written or recorded information in their possession for 25 months after notice of action, including any notice of adverse action taken.(202.12)

Business Credit

All credit extended for business, commercial or agricultural purposes is subject to the general rule that a creditor may not discriminate against any applicant on a prohibited basis with respect to any aspect of a credit transaction.(202.4) The following special provisions also apply to business credit:

- Marital status may always be asked in business credit, but sex may not.
- The provisions requiring a bank to determine whether accounts are shared with spouses in order to furnish credit information are not applicable.
- The bank must provide the notifications relating to adverse action in business credit only when the applicant requests in writing the reasons for such action. The request must come within 30 days after oral or written notification that adverse action was taken.
- Any records relating to an application for business credit must be retained for 25 months after notice of action taken only if the applicant requests in writing within 90 days after adverse action is taken that such records be retained.
- If credit is applied for in the name of a business firm, a bank may insist that the firm name be used.(202.3(e))

The provisions regarding signature requirements are applicable to business credit. Banks generally may not require that spouses of principals become liable on or guarantee a debt unless the spouse is also a principal in the business and the bank has a general policy of requiring all principals to sign.(202.7(d)) In all other respects, Regulation B applies to business credit, and the discussions in the preceding paragraphs are applicable.

Consumer Leases

On January 24, 1984, the United States Court of Appeals, Ninth Circuit, ruled that the Equal Credit Opportunity Act (ECOA) applies to consumer leases as defined by the Consumer Leasing Act, 15 U.S.C. 1667(1). The court's decision states, "Because the language of the ECOA is broad and its antidiscriminatory purpose is overriding and because the Consumer Leasing Act and ECOA are part of a comprehensive umbrella statute [Consumer Credit Protection Act] designed to protect the interest of consumers, we conclude that the ECOA applies to consumer leases." [Brothers v. First Leasing, 724 F.2d 789 (1984)] This ruling reverses informal staff opinions issued by the Federal Reserve Board and the Federal Trade Commission. It is binding in all states under the jurisdiction of the Ninth Circuit (Alaska, Arizona, California, Hawaii, Idaho, Montana, Nevada, Oregon and Washington).

In view of the ruling, examiners should review banks' consumer lease transactions for conformance to the general anti-discriminatory provisions of the ECOA. Although the ruling is binding only in those states in the Ninth Circuit, all banks should be cognizant of the risk if courts in their areas reach a similar conclusion. It is prudent for banks located in all states to take appropriate measures to minimize risks associated with consumer lease transactions.

RELATIONSHIP TO STATE LAW

Regulation B alters, affects or preempts only those state laws that are inconsistent with the ECOA or Regulation B, and then only to the extent of the inconsistency. Whether a state law is inconsistent may be determined by reviewing section 202.11(b)(1). In case of doubt, a formal Federal Reserve Board interpretation may be requested. Any person may apply for an interpretation pursuant to the requirements of section 202.11(b)(2). The regulation does not alter any provision of state property laws or federal or state banking regulations which deal with the solvency of financial institutions or laws relating to the disposition of decedents' property.

PENALTIES AND LIABILITIES

The ECOA provides for punitive damages of up to $10,000 in individual suits and the lesser of $500,000 or one percent of the creditor's net worth in class action suits, in addition to actual damages. Successful complainants will also be awarded court costs and attorneys' fees.(15 U.S.C. 1691e)

POLICY STATEMENT

The Corporation, along with the other federal financial institution regulators, has adopted the "Equal Credit Opportunity and Fair Housing Acts Enforcement Policy Statement." The objective of the statement is to ensure that the rights of credit applicants are protected by requiring creditors to take corrective action for certain serious violations. Whenever such violations are discovered, the Corporation will require the bank to take action to ensure that the violations will not recur and to correct their effects. Violations of the ECOA in the following areas are considered serious and will usually be subject to retrospective corrective action:

- Discouraging applicants on a prohibited basis;
- Using credit criteria in a discriminatory manner in evaluating applications;
- Imposing different terms on a prohibited basis;
- Requiring cosigners, guarantors or the like on a prohibited basis;
- Failing to furnish separate credit histories as required; and
- Failing to provide an adequate notice of adverse action.

II-A
Section

Retrospective corrective action will generally be required for violations that occurred within 24 months prior to discovery except for violations concerning adverse action notices where the corrective action period is six months prior to discovery.

EXAMINATION OBJECTIVES

1. To determine whether the bank has engaged in actions which treat or have the effect of treating one applicant less favorably than another on a prohibited basis.
2. To determine the adequacy of the bank's policies, procedures, and internal controls for compliance with Regulation B.
3. To determine the bank's compliance with the provisions of Regulation B in:
   - The application process;
   - The evaluation of applications;
   - Action taken on applications or accounts; and
   - The furnishing of information and the retention of records on accounts.

EXAMINATION PROCEDURES

Limited and Expanded Review

1. Review any written loan policies, procedures, guidelines, etc., including collateral requirements and standards, applicable to each type of credit offered. If written policies are not available, determine what policies and procedures are followed in practice through interviews with management and lending staff. Analyze these policies and procedures to determine if any discriminatory practices are evident. The analysis should include an evaluation of whether any of the policies or procedures fail the "effects test."(202.4)

2. Obtain any complaints concerning the lending function that the bank may have received since the last examination. Review these complaints and their resolution to identify any possible problem areas in the bank's policies or procedures and investigate further as necessary. Determine if any of the complaints warrant an in-depth credit discrimination complaint investigation.

3. Interview personnel who respond to written or oral loan inquiries or take applications to determine that no statements are made to a prospective applicant that would, on a prohibited basis, discourage a reasonable person from applying.(202.5(a))

4. Review all blank loan application forms, credit scoring sheets, financial statement forms and any other forms used to secure personal information on a borrower. Ensure that prohibited items of information are not requested and that any request for "other income" is properly qualified.(202.5)

5. For the various types or categories of credit or loans extended:

   - Review a sample of notes and files on credit extended to minorities and non-minorities and compare the terms of these credits to the bank's written and/or oral policies to determine consistency of treatment.

   - Review a sample of rejected credit applications, with particular emphasis on applications from women and minorities. Determine whether the information available on the records is consistent with and supports the reasons for denial stated on the adverse action notices, that the reasons for rejection are consistent with the bank's written and/or oral policies as previously determined and were applied consistently to both minority and non-minority applicants.(202.4)

6. Determine that no prohibited information appears in the files, was considered in evaluating an application, or was used as a basis in denying a loan.(202.4)

7. Determine that information concerning the spouse of an applicant is obtained only where permitted.(202.5(c))

8. Determine whether childbearing intentions or capabilities are considered.(202.5(d)(4))

9. Determine whether the bank considered all income to the extent that it will continue and does not discount income on a prohibited basis.(202.6(b)(5))

10. Determine whether credit history, when used by the bank, is considered in accordance with applicable requirements.(202.6(b)(6))

11. Determine whether applications for individual accounts are not refused because of the applicant's sex, marital status or other prohibited basis.(202.7(a))

12. Determine whether applications for accounts in birth-given names are accepted.(202.7(b))

13. Determine through a sample of applications and loan documents whether the spouse of an applicant was requested or required to sign any instrument and, if so, whether the signature was obtained as permitted.(202.7(d))

14. Where a cosigner, guarantor, endorser, etc. was required, determine whether the choice of the second party was left to the applicant.(202.7(d)(5))

15. Determine whether accurate notifications of adverse action were given to applicants within the time required.(202.9)

16. If the bank furnishes credit information to other parties, determine that such information is properly reported for joint accounts held by married persons.(202.10)

17. Review the bank's file for credit advertisements. Determine that the advertisements were nondiscriminatory i.e., did not suggest or imply a preference or discourage prospective applicants on a prohibited basis.

18. Determine whether required records are maintained for 25 months.(202.12)

FAIR HOUSING

INTRODUCTION

The Fair Housing Act (FHA) is Title VIII of the Civil Rights Acts of 1968. The fair housing lending provisions of the FHA (42 U.S.C. 3605) prohibit discrimination in all aspects of the financing of housing. More specifically, section 805 of the FHA makes it illegal for a bank to deny a loan for the purpose of purchasing, constructing, improving, repairing, or maintaining a dwelling, or to discriminate in fixing the amount, interest rate, duration, or other terms or conditions of such loan because of the race, color, religion, sex, or national origin of the applicant, any person associated with the applicant in connection with the loan or the purposes of such loan or the present or prospective owners, tenants, or occupants of the dwelling or dwellings in relation to which the loan is to be made.

DISCRIMINATION IN HOUSING-RELATED LENDING

Indications of Possible Discrimination

Discrimination in housing-related lending is rarely clear cut. Consequently, it is incumbent on the examiner to pursue indications of possible discrimination whenever they are noted. Such indications include the following:

- A lack of applications from protected group members and/or from census tracts and neighborhoods with relatively large percentages of protected group members.
- A disproportionate number of applications from protected group members that are withdrawn.
- A disproportionate number of denials of applications from members of protected groups.
- Branches located in areas with high percentages of protected group members that either do not have mortgage loan applications available or do not take applications.
- Delays in acting on applications submitted by protected group members.
- None or few minorities represented among the staff in an office even though minorities account for a significant portion of the local community.
- Refusing to lend conventionally in certain geographic areas and instead restricting those areas to VA and FHA loans only.

Whenever such practices of conditions are encountered, the examiner should investigate thoroughly the reasons or causes.

Effects Test

Under the "effects test" concept, conduct which has a disproportionate adverse impact on a protected group or which has the effect of perpetuating segregated housing may constitute unlawful discrimination, regardless of intent. Policies or practices which appear objective and neutral on their face may nevertheless be illegal if they result in the rejection of a higher proportion of credit applications received from minorities and/or women or result in the imposition of more onerous credit terms on a higher proportion of minority and/or women borrowers. If such disproportionate adverse effect is shown, the bank has the burden of proving that the particular policy or practice is justified by "business necessity" and that a less discriminatory means of achieving the same objectives does not exist.

Some policies or practices which may raise "effects test" questions include, but are not limited to, the following:

- A requirement that the property securing a mortgage loan must not exceed a particular age, or appraisal practices which establish unrealistically low values for older properties.
- Restricting mortgage lending to loans for certain types of properties, such as single-family homes, properties having no more than two floors, those with large lots, garages, or with large square footage requirements.
- A policy of not making loans on properties in certain locations or appraisal practices which arbitrarily discount the value of a property because of its location.
- A policy of making mortgage loans only to applicants who have previously owned a home.
- Establishing highly restrictive downpayment or income requirements, e.g., requiring a 25 percent downpayment or setting the maximum monthly mortgage payment to income ratio at 20 percent.
- Setting high minimum mortgage loan amounts that effectively exclude low-income borrowers or low maximum loan amounts that limit the bank's participation in the mortgage market.
- Arbitrarily discontinuing the making of FHA or VA mortgage loans.

The Fair Housing Act does not require a bank to make unsound loans or to provide more favorable terms because of an applicant's status as a member of a protected group. It does, however, require that credit decisions be based on economic factors applied equally to all applicants and that such decisions not violate the "effects test" in the particular circumstances.

II-B
Section

Policy Statement

The Corporation, along with the other federal financial institution regulators, has adopted the "Equal Credit Opportunity and Fair Housing Acts Enforcement Policy Statement." The objective of the statement is to ensure that the rights of credit applicants are protected by requiring creditors to take corrective action for certain serious violations. Whenever such violations are discovered, the Corporation will require the bank to take action to ensure that the violations will not recur and to correct their effects.

Violations of the FHA in the following areas are considered serious and will usually be subject to retrospective corrective action:

- Discouraging applicants on a prohibited basis;
- Using credit criteria in a discriminatory manner in evaluating applications;
- Imposing different terms on a prohibited basis; and
- Requiring cosigners, guarantors or the like on a prohibited basis.

Retrospective corrective action will generally be required to correct the conditions resulting from violations that occurred within 24 months prior to discovery.

PART 338—FAIR HOUSING

Purpose

In order to provide the monitoring data needed to analyze compliance with the fair lending provisions of the FHA, the Corporation adopted Part 338 effective July 3, 1978. The regulation requires banks that extend "home loans" to adhere to certain advertising, poster and recordkeeping requirements. A "home loan" is any extension of credit for the purchase, construction, refinancing, improvement, repair or maintenance of a one-to-four family dwelling at least one unit of which the applicant occupies or intends to occupy as his principal residence, and which secures or will secure the extension of credit.(338.1(f))

The regulation establishes recordkeeping requirements for insured state nonmember banks with respect to applications for home loans. An application is a written or an oral in-person request by an individual for a home loan which is received on the bank's premises by a bank employee authorized to receive such request. This definition excludes telephone requests.(338.1(b))

Advertising

The regulation requires that advertisements of home loans include a prominent indication that the bank makes such loans without regard to race, color, religion, sex or national origin. This requirement is met in written and visual advertisements by inclusion of a facsimile of the Equal Housing Lender logotype and legend. In oral advertisements, the bank must state that it is an "Equal Housing Lender."(338.2)

Equal Housing Lender Poster

Any bank that makes home loans must display the Equal Housing Lender Poster in any lobby and other area within the bank where deposits are received or home loans are made.(338.3)

Recordkeeping Requirements

Every bank that makes home loans is required to request and retain the following initial data on each home loan applicant:

- Date of application;
- Name;
- Address;
- Location of property;
- Sex;
- Race/national origin;
- Age; and
- Marital status.(338.4(a))

If the bank has an office in a primary metropolitan statistical area ("PMSA"), a metropolitan statistical area ("MSA"), or a consolidated metropolitan statistical area ("CMSA"), and had assets exceeding $10 million as of the previous December 31, numerous additional items of information are required to be requested from applicants, including loan type and disposition, data on employment, income, number of dependents, assets and liabilities, monthly payments on liabilities and various characteristics of the loan and property.(338.4(a)(2)) (Virtually all of this data is requested on the standard Residential Loan Application form contained in Appendix B to Equal Credit Opportunity Regulation B.) The bank is required, in addition, to maintain complete and accurate log-sheets containing the initial data requested from all applicants unless its assets did not exceed $50 million as of December 31 of the preceding calendar year and it received fewer than 25 home loan applications during that year.(338.4(a)(2)(iv))

Disclosure

The bank is required to disclose to the applicant that the data regarding race/national origin, marital status, age and sex is being requested to enable the FDIC to monitor the bank's compliance with the ECOA and the FHA. The bank is also required to disclose that, should the applicant not provide his/her race/national origin and sex information voluntarily, the bank must note the information on the basis of visual observation or surname.(338.4(b))

Record Retention

The monitoring information requested from applicants is required to be retained by the bank for 25 months after the bank notifies an applicant of action taken on an application.(338.4(c))

EXAMINATION OBJECTIVES

1. To determine whether the bank is adhering to nondiscriminatory lending practices.
2. To determine the adequacy of the bank's policies, procedures and internal controls designed to assure nondiscriminatory lending.
3. To determine the bank's compliance with the recordkeeping, advertising and poster provisions of Part 338.

EXAMINATION PROCEDURES

Limited Review

1. Review any written loan policies, procedures, guidelines, etc., including any written property appraisal policies or procedures and those governing collection and foreclosure practices. If written policies are not available, determine what policies and procedures are followed in practice through interviews with management and the lending staff. Analyze these policies to determine if any discriminatory practices are evident. The analysis should include an evaluation of whether any of the policies or procedures fail the "effects test."

2. Interview loan inquiry and application intake personnel to identify the extent to which procedures are written and/or well established and nondiscriminatory in nature and in use, particularly with regard to any prescreening practices. Compare responses to results of any outside contacts made for CRA purposes.

3. Interview loan officers and, where necessary, senior management officials: to verify that practices coincide with any written policies and procedures; to determine existing policies and procedures in the absence of written materials; and to identify the nature and extent to which the bank makes exceptions to existing policies and procedures. In particular, obtain a clear understanding of bank policy regarding minimum and maximum mortgage loan amounts; loan-to-value ratios; mortgage payment-to-income and total debt payments-to-income ratios; any other analytical ratios used; requirements on nature and length of employment; credit history and property underwriting standards.

4. Obtain any complaints concerning housing lending that the bank may have received since the last examination. Review these complaints and their resolution to identify any possible problem areas in the bank's policies or procedures and investigate further as necessary.

5. Review a sample of notes and files for home loans granted to minorities and non-minorities and compare the terms of these loans to the bank's written and/or oral policies and to each other to determine consistency of treatment. This review should incorporate characteristics detailed on the Home Loan Worksheet.

6. Review a sample of rejected home loan applications, with particular emphasis on applications from women and minorities. Determine whether the information available in the records is consistent with and supports the reasons for denial stated in the adverse action notices. Determine also that the reasons for rejection are consistent with the bank's written and/or oral policies as previously determined and were applied consistently to both minority and non-minority applicants.

7. For HMDA banks, where applicable select a sample of entries on the bank's log-sheets and compare these entries to the relevant source documentation. Determine that the information reflected on the log-sheets is reasonably accurate and complete.(338.4(a)(2)(iv))

8. Ascertain compliance with the other applicable recordkeeping requirements, including proper disclosure of the reason for requesting monitoring information and the bank's obligation when requested data is not voluntarily furnished.(338.4)

9. Review the bank's advertising file for home loan advertisements. Determine that the advertisements were nondiscriminatory (i.e., did not suggest or imply a preference on the prohibited basis) and that the "Equal Housing Lender" logotype was properly utilized. In assessing the nondiscriminatory character of the bank's advertising practices, consider the readership or audience of the publications or other media in which the advertisements appeared.(338.2)

10. Determine that the bank is displaying the Equal Housing Lender Poster in an acceptable manner where required.(338.3)

Expanded Review

1. Review any written mortgage loan policies, procedures, guidelines, etc., including any written property appraisal policies or procedures and those governing collection and foreclosure practices.

2. Interview loan inquiry and application intake personnel to identify the extent to which procedures are written and/or well established and nondiscriminatory in nature and in use, particularly with regard to any prescreening practices. Compare response to results of any outside contacts made for CRA purposes.

3. Interview mortgage loan officers and where necessary, senior management officials: to verify that practices coincide with any written policies and procedures; to determine existing policies and procedures in the absence of written materials; and to identify the nature and extent to which the bank makes exceptions to existing policies and procedures. In particular, obtain a clear understanding of bank policy regarding minimum and maximum mortgage loan amounts; loan-to-value ratios; mortgage payment-to-income and total debt payments-to-income ratios; any other analytical ratios used; requirements on nature and length of employment; credit history and property underwriting standards.

4. Identify any policies of procedures which though nondiscriminatory on their face, may have a disproportionate adverse impact on minority and/or women applicants in the bank's community. Consider the demographics, economic conditions and type and age of housing stock in the community.

5. For HMDA banks, where applicable, review the log-sheets for completeness, particularly regarding race and sex codes and disposition columns. If the log-sheets are so poorly maintained as to make it impossible to do a comprehensive analysis, note that fact for corrective action.

6. From the log-sheets or other bank records as available, compare a sample (the size of which should depend upon the volume of home lending) of rejected and accepted minority and/or female applications as appropriate with a similar sample of applications received from white males and couples (control group) for possible disparate treatment. In addition to the accept/reject decision, terms to be compared include, but are not limited to, interest rates, points and other prepaid finance charges, repayment terms including maximum maturities, required downpayments and whether a cosigner was required. Ascertain whether the requirements for similarly qualified minority/female applications were more rigorous than those for the control group. The sample Home Loan Worksheet included at the end of this section should be used for this analysis.

   Determine for the cases reviewed that the information available in the loan files is consistent with and supports the reasons for denial stated in the adverse action notices, that the reasons for rejection are consistent with the bank's policies and procedures as previously determined, and that the policies and any exceptions were applied consistently to both minority/female and non-minority applicants. Set aside questionable cases for discussion with responsible loan officers.

7. Identify the location of the bank's local community or communities. Using the most recent demographic tables, determine whether any census tract within such communities has a percentage of Black, Hispanic or other minority households equal to or greater than 10 percent. If so, develop an estimate of the percentage of Black, Hispanic or other minority households in the community. Enter on a Log Analysis Worksheet. (See the sample Log Analysis Worksheet provided at the end of this section.) Note in particular the apparent demand for home loans based on the data available from the HMDA aggregation tables. (See the sample HMDA aggregation table for CINCINNATI, OH-KY-IN SMSA at the end of this section.) Investigate any apparent shortage of applications from Blacks, Hispanics, or other minorities.

8. Assuming substantially complete log-sheets, where applicable, complete a Log Analysis Worksheet for all home loan applications received during the past 12 months that have reached the disposition stage. Proceed as follows:

   - If the percentage of rejected minority or female applicants significantly exceeds the percentage of rejected control group applicants, investigate the reasons.
   - Analyze the volume and group distribution of accepted and rejected applications. Investigate any apparent disparities.
   - Where the percentage of rejected minority applicants significantly exceeds the percentage of control group applicants, particularly where the bank's local community or communities includes census tracts having substantial percentages of minority residents, review the bank's most recent HMDA-1 form (or state equivalent) in conjunction with the most recent demographic tables to determine whether there is evidence of a pattern or practice of not making loans in census tracts having significant percentages of minority residents. If such a pattern or practice emerges:
     - Determine why the bank has made a practice of not lending in the particular areas and the

limitation(s) on and the reason(s) for any such practice.

From the sample previously developed, review loan files on rejected applications for loans on properties located in minority census tracts. Evaluate in particular the nature of any comments made in the appraisal if rejection is based on condition of the property or the condition of surrounding properties. If rejection is based on factors other than property, evaluate to determine if such factors had the effect of discriminating against a protected group on a prohibited basis.

9. Ascertain that the bank is in compliance with the recordkeeping, advertising and poster provisions of Part 338, as detailed in the limited review procedures.

HOME MORTGAGE DISCLOSURE

INTRODUCTION

Congress enacted the Home Mortgage Disclosure Act (HMDA) (12 U.S.C. 2801 et seq.) in 1975. The HMDA became effective, along with implementing Regulation C, on June 28, 1976. In 1980, the HMDA was amended and extended for a five-year period under provisions of the Housing and Community Development Act. A corresponding revision of Regulation C was adopted by the Federal Reserve Board effective December 30, 1981. More recently, the HMDA was extended to September 30, 1987 by Public Law 99-430.

The HMDA grew out of public concern over credit shortages in certain urban neighborhoods. The Congress found that some depository institutions had contributed to the decline of certain geographic areas by their failure, pursuant to their chartering responsibilities, to provide adequate home financing to qualified applicants on reasonable terms and conditions.

The purpose of the HMDA and Regulation C is to provide the public with information that will help show whether depository institutions are serving the housing credit needs of the neighborhoods and communities in which they are located. Another purpose is to help public officials distribute public sector investments in a way that will attract private investments in neighborhoods where they are needed.

As its name implies, the HMDA is a disclosure law and relies upon public scrutiny for its effects. It does not prohibit any specific activity of lenders, and it does not establish a quota system of mortgage loans to be made in any Metropolitan Statistical Area/Primary Metropolitan Statistical Area (MSA/PMSA) or county. What it does do is allow the public to review a lender's mortgage loan record in a particular area. The public must then form a judgement about that lender's responsiveness in providing adequate home financing.

The HMDA requires that certain loan data be made available to the public at the institution and at central data repositories, one in each MSA/PMSA. In addition, the Federal Financial Institutions Examination Council (FFIEC) must aggregate and make available at the central data repositories the loan origination data for all institutions in the MSA/PMSA, showing lending patterns by location, age of housing stock, income level, and racial characteristics. These aggregation tables for insured nonmember banks are available at the Regional Offices. A sample aggregation table is at the end of the Fair Housing Section II-B.

INSTITUTIONS COVERED

Regulation C applies to institutions that meet all of the following requirements, with the exception of state-chartered institutions in a state granted an exemption by the Federal Reserve Board:

- Total assets of more than $10 million on the preceding December 31.
- A home or branch office located in an MSA/PMSA so designated as of January 1.
- The institution makes federally related mortgage loans.[1]

In addition to insured nonmember banks, the Corporation has enforcement responsibility for certain noninsured depository institutions.(12 U.S.C. 2804(b)). However, industrial banks (insured or noninsured) are not covered because these institutions are not one of the types specifically mentioned in the HMDA and Regulation C. (Opinion dated 4/7/86 by AGC Roger A. Hood.)

DATA TO BE COMPILED

An institution must compile data on the number and total dollar amount (i.e., original principal amount) of home purchase and home improvement loans that it originates or purchases for each calendar year. The following real estate loans are to be included in the compilation.

- Federal Housing Authority (FHA), Farmers Home Administration (FmHA), or Veterans Administration (VA) mortgage loans.
- Home improvement loans. This includes any loan, including a refinancing, (i) whose proceeds, as stated by the borrower to the lender at the time of the loan application, are to be used for repairing, rehabilitating, or remodeling a residential dwelling; and (ii) that is recorded on the institution's books as a home improvement loan.
- Home purchase loans. This includes any loan, including a refinancing, secured by and made to purchase residential real property (such as single-family homes or dwellings for two-to-four families, other multi-family dwellings, individual units of condominiums or cooperatives, and mobile homes when defined as real property under state law). The term does not include temporary financing (such as

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[1] An institution may be subject to the HMDA if it makes first-lien mortgage loans on one-to-four family dwellings and is either federally insured or regulated, originates loans that are insured or guaranteed by HUD or another federal agency, or intends to sell the loans to FNMA, GNMA or the FHLMC. An institution that makes second mortgage loans only is not covered and need not report.

a bridge loan or a construction loan) or the purchase of an interest in a pool of mortgage loans (such as mortgage participation certificates issued or guaranteed by the Federal Home Loan Mortgage Corporation, the Government National Mortgage Association or the Farmers Home Administration).

Regulation C requires the breakdown of the data into two categories depending upon the source of the loan, two categories depending on the location of the property, and five categories depending on the type of loan.

The two source categories are:

- Loans originated by the institution, that is, loans that the institution makes itself; and
- Loans originated by another lender and purchased by the institution.

The two location categories are:

- Loans for property located within each MSA/PMSA where the headquarters or a branch of the institution is located; and
- Loans for property located outside of any such MSA/PMSA.

The five type categories are:

- Loans to purchase one-to-four family dwellings insured or guaranteed by the Federal Housing Administration (FHA), Farmers Home Administration (FmHA) and Veterans Administration (VA);
- Conventional loans to purchase one-to-four family dwellings;
- One-to-four family home improvement loans;
- Home purchase and home improvement loans on multi-family dwellings (five or more families); and
- Non-occupant loans on one-to-four family dwellings.

Geographic Itemization

The loan data must be itemized by MSA/PMSA. Within each MSA/PMSA, the data must be further itemized by the census tract in which the property to be purchased or improved is located, except that:

- If the property is located in a county with a population of 30,000 or less (using 1980 census counts), itemization by county must be made instead of by census tract. An institution should also itemize loans by county if the property is in an area that has not been assigned census tract numbers on the maps in the "CENSUS TRACTS, PHC80-2" series.
- If the property is located outside any MSA/PMSA or is located in an MSA/PMSA in which the institution has neither a home nor a branch office, no itemization (by MSA/PMSA, county or census tract) is required and the data for all such loans must instead be listed in an aggregate sum.

Excluded Data

A depository institution must not disclose loan data for:

- Loans originated and purchased by the depository institution acting as trustee or in some other fiduciary capacity;
- Loans on unimproved land; or
- Refinancings that the institution originates if at the time of the refinancing there is no increase in the outstanding principal on the existing loan and the institution and the borrower are the same parties on the existing loan and the refinancing.

DISCLOSURE AND REPORTING REQUIREMENTS

A depository institution must make its loan data disclosure statements available to the public by March 31 following the calendar year for which the data were compiled, and must continue to make them available for five years from that date at the offices indicated below:

- A complete disclosure statement at its home office; and
- A disclosure statement in at least one branch office in each MSA/PMSA where the institution has offices, other than the MSA/PMSA in which the home office is located. The statement at a branch office may omit, at the option of the institution, all data other than the data relating to property located in the MSA/PMSA where that branch is located.

A depository institution must make its loan data disclosure statements available to anyone requesting them, for inspection or copying, during the hours the office is normally open to the public for business. A depository institution that provides photocopying facilities may impose a reasonable charge for copying service.

A depository institution must also provide notice of the availability of its mortgage loan data by posting a notice in the lobbies of its home and branch offices that are located in MSA/PMSA.

For purposes of data aggregation and availability at the central data repositories, a depository institution must send two copies of its complete disclosure statement to the appropriate FDIC Regional Office by March 31 following the calendar year for which the data were compiled. The Federal Reserve Board's "Guide to HMDA Reporting" provides guidance to help depository institutions comply with the reporting requirements of the HMDA.

SPECIAL SITUATIONS

- Free-standing automated teller machines and other electronic terminals are not considered a branch office.
- An institution may categorize a first-lien loan made for home improvement as a home purchase loan if that is the manner in which it normally records first-lien loans.
- Institutions may not use ZIP codes in lieu of census tract designations. Untracted areas must be reported in the county itemization.
- Loans that are originated by an institution in a fiduciary capacity may not be reported.
- The purchase of an interest in a pool of mortgage loans, such as mortgage participation certificates, may not be reported.
- For home improvement loans, whether originated or purchased, the amount to be reported may include unpaid finance charges.
- First lien mortgage assumption loans should be reported as home purchase loans.
- A bank that makes only home improvement loans that are not first-lien loans is not covered by the regulation.

ADMINISTRATIVE ENFORCEMENT AND SANCTIONS FOR VIOLATIONS

Compliance with the HMDA and Regulation C is enforced by the Comptroller of the Currency, the Federal Reserve Board, the Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board, and the National Credit Union Administration.

An error in compiling or disclosing required data is not considered a violation of the HMDA or Regulation C if the error was unintentional and resulted from a bona fide mistake despite the maintenance of procedures reasonably adapted to avoid such an error. There is no civil or criminal liability for violations.

II-C
Section

EXAMINATION OBJECTIVES

1. To determine if the depository institution complies with the reporting requirements of the HMDA and Regulation C.

2. To determine the adequacy of the institutions's policies, practices or internal controls to assure compliance with the HMDA and Regulation C.

EXAMINATION PROCEDURES

Limited and Expanded Review

1. Determine whether the depository institution:
   - Makes federally related mortgage loans on one-to-four family dwellings.(203.2(c))
   - Had more than $10 million in assets as of December 31 of the previous year.(203.3(a)(1))
   - Has a home or branch office in an MSA/PMSA.(203.3(a)(2))
   - Is not exempt on the basis of similar state law.

If the depository institution meets all of the above criteria, perform the following steps.

2. Test for compliance with written policies and internal controls:
   - Determine how the institution ensures that home mortgage loan information is properly compiled and disclosed.
   - Determine how management ensures that affected institution personnel are aware of the requirements of the HMDA.
   - Determine if the institution maintains the necessary records to compile the required disclosure statement.
   - Determine if the policies, procedures and training are adequate, on an ongoing basis, to ensure compliance with the HMDA.
3. Determine: (1) if the institution is using the correct HMDA-1 form or format, and (2) if the appropriate Bureau of Census data is being used to correctly compile the data.(203.4(b) and (d))
4. Determine through review and discussion with the responsible officer if the institution has accurately compiled home mortgage disclosure information.
5. Determine if the institution has posted the notice of availability in the lobbies of its home and branch offices that are located in SMSAs.(203.5(d))
6. Determine whether the loan disclosure statement is available in the home office and at least one branch office located in each MSA/PMSA (other than the home office MSA/PMSA).(203.5(b))
7. Determine whether the institution makes loan disclosure statements available by March 31 following the calendar year for which the data were compiled to anyone requesting to inspect and/or copy them.(203.5(a) and (c))
8. Determine if the institution has forwarded two copies of the disclosure forms to the Regional Office by March 31 following the calendar year for which the data were compiled.(203.5(e))
9. Determine if HMDA statements are being retained for a five-year period.(203.5(a))

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Section

EXAMINER CHECKLIST

Home Mortgage Disclosure	Yes	No
1. Did the institution make any federally related mortgage loans on one-to-four family dwellings? (203.2(c))	____	____
2. Did the institution have assets of more than $10 million as of December 31 of the preceding year? (203.3(a)(1))	____	____
3. Does the institution have a home or branch office in a MSA/PMSA? (Sec. 203.3(a)(2))	____	____

(If all of the answers to questions 1, 2 and 3 are "yes," the institution is subject to the HMDA, unless exempt by virtue of a similar state law, and the examiner may complete the following checklist.)

	Yes	No
4. Is the institution ensuring that the home mortgage loan information is properly compiled and disclosed?	____	____
5. Does management ensure that affected bank personnel are aware of the requirements of the HMDA?	____	____
6. Does the institution maintain the necessary records to compile the required disclosure statement?	____	____
7. Does management ensure that information is disclosed accurately?	____	____
8. Are policies, procedures and training adequate, on an ongoing basis, to ensure compliance with the HMDA?	____	____
9. Is the correct HMDA-1 form or format being utilized? (203.4(b))	____	____
10. Is the necessary census tract information available for compilation of data?(203.4(d))	____	____
11. Is the institution compiling the HMDA-1 according to Regulation C?(203.4)	____	____
12. Are the census tracts and/or county designations accurate?(203.4(d))	____	____
13. Has the institution posted notices in the lobbies of its home and branch offices that are located in MSA/PMSAs on the availability of the HMDA statement? (203.5(d))	____	____
14. Is the HMDA statement available at the home office and at least one branch office, if any, in each MSA/PMSA (other than the home office MSA/PMSA)? (203.5(b))	____	____
15. Are the HMDA statements available to anyone requesting them for inspection or copying, during normal public hours?(203.5(c))	____	____
16. Are HMDA statements retained for five years?(203.5(a))	____	____
17. Was the latest disclosure statement available to the public by March 31 following the calendar year for which the data were compiled?(203.5(a))	____	____

	Yes	No
18. Did the institution forward two copies of the HMDA forms to the Regional Office by March 31 following the calendar year for which the data were compiled? (203.5(e))	______	______
19. Is the institution complying with all other requirements of Regulation C?	______	______

COMMUNITY REINVESTMENT

INTRODUCTION

The Community Reinvestment Act (CRA) (12 U.S.C. 2901 et seq.) is intended to encourage banks to help meet the credit needs of their entire communities, including low- and moderate-income neighborhoods, while preserving the flexibility necessary to operate in a safe and sound manner.

Encouragement is to be provided by the Corporation which is required to:

- Use its examination authority to encourage a bank to help meet the credit needs of its entire community, consistent with the safe and sound operation of the bank;
- Assess, in connection with its examination, the bank's record of helping to meet the credit needs of its entire community; and
- Take that record into account in evaluating an application for deposit insurance, a branch or other deposit facility, office relocation or merger.

Proponents of the CRA were concerned, among other things, with situations in which local lenders reportedly exported local deposits to other areas despite sound local lending opportunities. Such disinvestment was considered a threat to community and neighborhood vitality. Lenders, therefore, are encouraged to give particular attention to local housing and development needs of urban and rural areas. Increased lender sensitivity to such needs would help preserve, rehabilitate and revitalize such areas. Moreover, even though credit for local housing and community development was emphasized, it was realized that other types of credit provide community facilities and services necessary for neighborhood vitality and, more generally, a healthy local community.

The CRA is not intended to inject hard and fast rules or ratios into the examination or application process. Rather, the law contemplates a judgmental evaluation of a lender's record in order to accommodate varying circumstances. Nor does the CRA require banks to make high risk loans that jeopardize their safety. Rebuilding and revitalizing communities are viewed as beneficial for both communities and banks.

PART 345 - COMMUNITY REINVESTMENT

The Corporation's implementing regulation (Part 345) requires the board of directors of each insured nonmember bank to adopt and, at least annually, review a CRA statement. The statement must include: (1) a delineation on a map of each local community served by the bank, (2) a list of the specific types of credit the bank is prepared to extend within each local community, and (3) a copy of the CRA notice. The regulation also encourages each bank to include in its statement a description of its efforts to ascertain and help meet community credit needs.

A bank must provide in each office a CRA notice, the exact wording of which is prescribed in the regulation. The public notice indicates that the CRA statement is available, that written comments on the statement and the bank's community lending performance may be submitted to the bank or the Corporation, that a file of such comments is publicly available, and that the public may request announcements of applications covered by the CRA from the Corporation. Each bank must keep a public file of CRA statements in effect and CRA-related public comments received during the past two years.

The CRA regulation sets forth a list of factors which the Corporation will consider in assessing each bank's record of helping to meet community credit needs, including those of low- and moderate-income neighborhoods. Banks are not required to adopt particular activities on the list since the regulation is designed to allow each bank considerable flexibility in determining how it can best help to meet the credit needs of its entire community in view of its particular skills and resources.

In essence, the regulation encourages banks to become aware of the full range of credit needs of their communities and to offer the types of credit and credit-related services that will help meet those needs. However, the regulation does not require banks to offer particular types or amounts of credit. The Corporation's assessment of a bank's CRA record will be taken into account by the Corporation in evaluating a variety of applications.

BACKGROUND FOR EXAMINATIONS

Judgmental Process

In conducting a CRA examination, the examiner is expected to adjust the CRA procedures on a case-by-case basis to accommodate banks that vary in size, expertise and locale. Community credit needs will often differ with the specific characteristics of each local community, and a bank should be evaluated on the basis of its attempts to ascertain, its determination to help meet, and its performance in helping to meet community credit needs in the context of its resources and local circumstances.

Balanced Viewpoint

The examiner should maintain a balanced perspective in conducting a CRA examination. The examiner cannot normally conclude on the basis of any one factor that a bank is or is not helping to meet the credit needs of its local community or communities. Nor can the examiner adequately assess a bank's performance on the basis of any one source of information, data or opinion. For that reason, the examination procedures are designed to ensure that information from both the bank and the community is objectively reviewed and evaluated.

Bank's Input

The examination procedures give each bank the opportunity to demonstrate that it is having a beneficial influence on its local community or communities. Bankers that are helping to meet community credit needs are proud of that fact and will be of substantial assistance to the examiner in assessing the performance of their banks.

Examiner Encouragement

When appropriate, an examiner should encourage a bank to improve its CRA record by discussing with management various ways in which the bank may strengthen its performance. The examiner should not, however, insist on any specific action by the bank, such as the making of a certain type of loan, which would interfere with the bank's responsibility for establishing its own policies.

Examination Burden

The examiner must be careful to not unduly burden the bank since Congress did not intend to impose significant new reporting or recordkeeping requirements on banks. The examiner should normally request only required records and other existing information, but the scope of the review must always be sufficient for an adequate assessment.

Bank's Financial Condition and Size, Legal Impediments and Local Economic Conditions

A bank's ability to help meet community credit needs is influenced by its financial condition and size, as well as by any legal impediments and the local economic conditions under which it operates. An examiner must take these considerations into account in assessing the bank's performance and in providing encouragement.

Technical Compliance with the Regulation

The examiner will check for compliance with the specific requirements of the regulation. However, compliance with procedural requirements does not imply that the bank has been serving local credit needs. The converse is also true: noncompliance with a technical requirement does not necessarily mean that the bank is not helping to meet community credit needs. The examiner must not lose sight of the intent of the statute in checking for technical compliance with the regulation. The entire examination is designed primarily to determine the extent to which the bank has helped and is helping to meet community credit needs.

Communication, Community Development and Low- and Moderate-Income Neighborhoods

In assessing the record, the examiner should bear in mind the special emphasis placed on effective communication and community development activities. With respect to communication, the premise is that community needs which can be met on a safe and sound basis are more likely to be met when the community is aware of the types of credit available and the lender is well informed about community credit needs. Hence, efforts to ascertain community credit needs and to publicize available credit services, including measures to identify the credit needs of, and to advertise in, low- and moderate-income neighborhoods, are encouraged. The examiner is authorized to conduct interviews with community members when such action would be appropriate in determining community awareness of the bank's credit services and local perception of credit needs.

The CRA also focuses on activities that foster development within the entire community, including low- and moderate-income neighborhoods. Consequently, housing-related extensions, participation in community development programs, and small business financing, including loans to small farms, are viewed favorably.

SELECTED FEATURES OF CRA EXAMINATIONS

The CRA Statement

A bank must prepare a separate CRA statement for each local community it serves, including a delineation of the relevant local community. It does not necessarily follow, however, that the statement prepared for each local community must contain a unique list of available credits. A bank serving several local communities may elect to prepare statements that contain lists of credits which are similar or identical for the local communities served. Since some credit needs are common to many local communities, such an approach would be consistent with the intent of CRA. There are other ways for a multi-community bank to satisfy this requirement. The examiner need not be especially concerned with the specific method employed by a multi-community bank so long as it makes a good faith effort to inform members of each local community about their community's boundaries and the types of credit extended there.

Reasonableness of Community Delineation

Each bank must delineate the local community or communities that it serves. For instance, a statewide branching bank would serve a number of "local communities," the total of which would constitute its "entire community." Further, more than one office of a bank may serve the same local community. For example, a bank may have offices throughout a city and its suburbs and consider that entire metropolitan area to be the local community for those offices. Each community delineation must, of course, include the contiguous areas surrounding each office or group of offices.

Because many factors influence the size and shape of a bank's community, the regulation provides guidelines to assist each bank in defining its local community or communities.

The first guideline suggests the use of widely recognized existing boundaries such as those of MSAs or counties for delineating a bank's local community or communities. Such boundaries frequently constitute a reasonable approximation of a bank's local community.

In general, a local community based on existing boundaries should be no larger than an entire MSA or a county in a non-MSA area. If a bank has offices in more than one such area, it will have more than one local community. When a bank has an office near the boundary of an MSA or county, it should include those portions of adjacent counties that it serves. In rural areas, a local community may sometimes encompass more than one county but, generally, banks should not use states or regions of states to delineate local communities. A small bank that serves an area smaller than an MSA or county may define its community to be a part of the MSA or county. A bank may make adjustments in a community delineation in the case of areas divided by state borders, significant geographic barriers, or areas that are extremely large or of unusual configuration.

The second guideline proposes the use of effective lending territory, a concept more familiar to savings and loan associations than to commercial and mutual savings banks. The effective lending territory is that local area or areas around each office or group of offices where an institution makes a substantial portion of its loans and all other areas equally distant. If a bank employs its effective lending territory, it is encouraged to follow existing boundaries where practical.

One should not conclude from this guideline that each office necessarily serves a separate and distinct local community because each office typically has a different, though possibly partially overlapping, effective lending territory. If a bank is represented throughout a trade or market area, it may be more reasonable to use that area as its local community.

Finally, the regulation allows a bank to use any other reasonably delineated area. A bank is thus given substantial leeway in specifying its local community so long as the definition is reasonable; that is to say, the bank can provide a sensible rationale for the delineation and has not arbitrarily excluded any low- and moderate-income neighborhoods.

Low- and Moderate-Income Neighborhoods

In determining whether the community definition is reasonable, the examiner must be alert to situations where low- and moderate-income neighborhoods are gerrymandered out of a delineated area. Moreover, in assessing the record of a bank, the examiner should focus particular attention on its performance in low- and moderate-income neighborhoods within a local community.

Low- and moderate-income neighborhoods may be identified in most cases in a manner similar to the approach taken by HUD in administering the Community Development Block Grant Program. For this purpose, such neighborhoods are approximated by those census tracts in an MSA where median family income is less than 80 per cent of median family income for the entire MSA.

Unfortunately, these data are not available for non-MSA counties. Non-MSA areas, especially rural areas, present a particular problem in identifying low- and moderate-income neighborhoods. In those areas, the examiner may have to rely on personal knowledge of the area, physical inspection as necessary, discussion with bank personnel or a combination of these.

Small Business Lending

Small business loans represent one type of credit which the Corporation believes is directly related to the purposes of the CRA. In considering small business lending, the examiner should not be concerned with any hard and fast or precise definition of what constitutes a small business. Instead, the examiner should regard as small business lending any loans to local firms whose access to credit is limited to local sources because of their size.

II-D
Section

EXAMINATION OBJECTIVES

1. To determine if the bank's policies address the intent of the CRA.
2. To encourage sensitivity and responsiveness to community credit needs.
3. To determine that the bank is complying with the requirements of the CRA regulation.
4. To determine the reasonableness of the bank's community delineation(s).
5. To assess the bank's record in helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with a safe and sound operation.
6. To develop, organize and report information on the bank's record for use in the supervisory and application processes.

EXAMINATION PROCEDURES

Limited Review

1. Determine the method used by the bank to delineate its local community or communities and the reasonableness of each such delineation.(345.3(a)) Note particularly any low- or moderate-income neighborhoods or areas that appear to have been arbitrarily excluded.

2. Assess the bank's record of performance in helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with its safe and sound operation. The various assessment factors detailed in the regulation should all be considered to the extent applicable to the particular bank and the community or communities in which it operates. HMDA data should be used to ascertain the volume and location of housing loans. Particular attention should be paid to the relative volume of lending in low- and moderate income areas.

   In assessing the record, the examiner should review the Officer's Questionnaire, review and analyze the bank's public file and interview responsible personnel to determine efforts undertaken by the bank to ascertain and help meet community credit needs. To the extent necessary for an adequate assessment, the examiner is encouraged to interview community members to determine community awareness of the bank's credit services and local perception of credit needs as well as the bank's efforts to meet those needs.

3. Review each CRA statement in effect during the past two years to determine that all required items are included.(345.4(b)) Note the specific types of credit the bank is prepared to extend within the local community and determine whether the types of credit in the CRA statement correspond with the types of credit actually being extended. Request an explanation of any difference.(345.4(b)(2))

4. Review minutes of directors' meetings to verify that all required CRA statements have been adopted, are reviewed at least annually and that the board has acted upon any interim changes and noted such actions in the minutes.(345.4(d))

5. Ascertain that the public file contains all signed comments received from the public that specifically relate to any CRA statement or to the bank's performance under the CRA as well as any responses made by the bank. The file should also contain all CRA statements in effect during the past two years.(345.5)

6. Ascertain that the bank's public notice contains the correct language and is properly posted.(345.6)

7. Review with management the following:
   - The extent to which the bank is helping to meet the credit needs of its community;
   - Suggestions that might better enable the bank to help meet the credit needs of its community;
   - Deficiencies or exceptions in policies or practices; and
   - Procedural violations of the regulation.

Expanded Review

1. Ascertain from bank personnel what steps the bank has taken or plans to take which indicate whether it is helping to serve the credit needs of its local community or communities.

2. Obtain the following:

   - Minutes of the board of directors' meetings, particularly those dealing with the adoption, review and revision of all CRA statements.

   - The bank's files of public comments and recent CRA statements.

   - Comment letters received by the Corporation.

   - The bank's loan and investment policy and procedural manuals, along with other manuals relating to the CRA.

3. Review minutes of directors' meetings and verify that the board has:

   - Adopted a CRA statement for each delineated community.

   - Reviewed each statement at least annually.

   - Acted upon any material change in each statement at the first regular meeting of the board following the change.

4. Review and analyze the public files for:

   - Any signed, written comments received from the public during the past two years that specifically relate to any CRA statement or to the bank's performance in helping to meet the credit needs of its community or communities. Determine that the comments do not contain any material specifically prohibited by the regulation. However, the comments themselves should be considered.

   - Any responses to the commentors that the bank may have made.

   - All CRA statements in effect during the past two years.

   Note: Inherent in the process of reviewing public files is the option of contacting commentors and/or community members to the extent deemed necessary.

5. Review each CRA statement in effect during the past two years and:

   - Ascertain if the bank's delineation of its local community or communities is reasonable. Give special attention to the following:

     —Considerations used by the bank to define its community.

     —Community boundaries that are sharply asymmetrical, too narrowly drawn or so broad that the bank fails to focus on its local community.

     —Whether any low- and moderate-income neighborhoods have been arbitrarily excluded.

     —Public comments specifically relating to the reasonableness of the bank's delineation(s).

     —Any relevant information obtained from other examination programs that have been performed.

     If a question remains regarding the reasonableness of the community delineation, a review of community boundaries drawn by comparable local banks may provide useful information.

   - Review and analyze the specific types of credits within certain categories that the bank is prepared to extend within the local community. Determine if the types of credit in the CRA statement correspond to the types of credit actually being extended by the bank. Request an explanation of any differences. If feasible and appropriate, review the list of available credits prepared by comparable local banks.

   - Determine that a copy of the CRA public notice is included.

   - Analyze any of the following optional information that the bank may have included:

     —A description of how its efforts, including special credit-related programs, help to meet community credit needs.

     —A periodic report regarding its record of helping to meet community credit needs.

     —A description of its efforts to ascertain the credit needs of its community, including efforts to communicate with members of its community regarding credit services.

     —Any other material the bank may have included.

6. Analyze the bank's policies, procedures and operating practices to determine if the bank:

   - Provides the CRA public notice in a manner specified by the regulation. (A bank may reprint this notice as a poster or flyer to be placed in its lobby. The notice requirement may also be satisfied by making the CRA statement, which includes the notice, available as a brochure in the lobby.)

- Makes all CRA statements available to the public as provided by the regulation.
- Makes the public comment files readily available for public inspection as provided in the regulation.

7. Review the bank's credit underwriting and appraisal criteria and the terms and conditions of loans to determine if they are being used for exclusionary purposes contrary to the objectives of the CRA.

8. Assessment Factors

- Activities conducted by the bank to ascertain the credit needs of its community, including the extent of the bank's efforts to communicate with members of its community regarding the credit services being provided by the bank.

  Ascertain from bank records and through interviews the extent to which the bank has communicated with members of its local community or otherwise has attempted to determine such needs. Pertinent factors may include:

  — Management review of written, signed comments received in response to the bank's CRA statement(s).

  — Studies conducted or reviewed by the bank concerning local credit needs.

  — The extent of the bank's efforts to communicate with members of its community regarding the credit services it is providing. Such members might include customers of the bank; educational organizations; merchants' associations; religious organizations; local government officials; block clubs; neighborhood organizations; coalitions of neighborhood organizations; local civil rights, consumer, minority, and non-English speaking groups; housing counseling service centers; community development corporations; nonprofit housing development corporations; and local development corporations.

  — The bank's communications with private organizations as may be identified by the Office of the Assistant Secretary for Neighborhoods, Voluntary/Associations and Consumer Protection at HUD.

  — The bank's review of the local government's Community Development Plan and Housing Assistance Plan prepared in conjunction with HUD's Community Development Block Grant Program.

  — Economic forecasting, as developed or used by the bank.

- The extent of the bank's marketing and special credit-related programs to make members of the community aware of the credit services offered by the bank.

  Review the bank's marketing program and determine if it is adequately designed to encourage applications for loans in its community, particularly in low- and moderate-income neighborhoods. Pertinent factors may include:

  — Any working relationships the bank may have with real estate brokers or others who service low- and moderate-income neighborhoods.

  — Mortgage counseling programs and programs of management assistance for small or minority businesses.

  — Development and participation in mortgage review boards.

  — Credit and credit-related services in low- and moderate-income neighborhoods compared to such services in other neighborhoods served by the bank.

  — Use of bank representatives for seeking out potential housing-related and small business demand in low- and moderate-income neighborhoods.

  — Advertising the types of loans the bank is willing to make in media likely to reach low- and moderate-income individuals in the bank's local community or communities.

  — Availability of convenient hours in offices accessible to residents of low- and moderate-income neighborhoods.

  — Use of informational brochures and participation in other educational efforts.

- The extent of participation by the bank's board of directors in formulating the bank's policies and reviewing its performance with respect to the purpose of the CRA.

- Any practices intended to discourage applications for types of credit set forth in the bank's CRA statement(s).

  Review other fair lending examination programs, particularly as they pertain to interviewing and prescreening. Additionally, ascertain the following:

- Whether administrative loan personnel and loan offices are aware of the CRA and the requirements of the implementing regulation.
- Whether lending officers are aware of the bank's delineation of its local community or communities and its policies, if any, with respect to its commitment to help meet the credit needs of its entire community, including low- and moderate-income neighborhoods.
- Whether loan officers are aware of the types of credit the bank offers to members of its local community or communities.
- Whether public contact personnel are aware of the availability of the bank's CRA statement(s) and files of public comments.
- Whether the bank is prepared to extend certain types of credit in some local communities or neighborhoods but not in others. An explanation of any difference should be requested.
- The extent to which the bank is willing to make loans in its delineated local community or communities, utilizing information derived below. Special attention should be given to the specific reasons why loan applications have been denied, whether or not such denial has been on a prohibited basis.
- Whether loan officers or other public contact personnel prescreen potential applicants from obtaining loans that the bank has stated it is willing to make, particularly applicants from low- and moderate-income neighborhoods.

- The geographic distribution of the bank's credit extensions, credit applications and credit denials.

Determine whether there is any indication of a geographic distribution of credit extensions, applications for credit and credit denials which would signify failure to serve selected areas of local communities, particularly low- and moderate-income neighborhoods. Initial reliance may be placed on discussion with other examiners, review of reports of examination and work papers from other examination programs performed. For those banks located in MSAs, additional reliance may be placed on other fair lending examination programs for ascertaining the volume and location of housing-relating credits. For loans made outside MSAs, particularly with respect to banks that are not located in such areas, interview management and review internal files to determine the extent of housing-related lending in low- and moderate-income neighborhoods and the extent to which the bank has not extended such credit in these areas.

Reliance may be placed upon geocoding of credit extensions, credit applications and credit denials. Where the bank is required to maintain logs of applications, the examiner should also review the logs to determine the geographic distribution of loans, applications and denials. In conjunction with other fair lending examination programs, it may be necessary to analyze further the geographic distribution of small business loans, including loans to small farms within the bank's local community.

- Evidence of prohibited discriminatory or other illegal credit practices.

Review prior Compliance Reports and, in conjunction with other examination programs, determine the extent to which the bank is currently complying with the law.

- The bank's record of opening and closing offices and providing services at offices.

Review the bank's record of and future plans for opening and closing branches and determine what factors management uses to determine which branches to close, which to leave open, and where to open new branches. The bank's approach can be determined through interviews with bank personnel knowledgeable about the bank's policy on opening and closing branches. Information can also be obtained through reviews of minutes of board of directors meetings, other bank records, Regional Office files, and interviews with representatives of public organizations with a particular focus on low- and moderate-income and minority neighborhoods. Also consider any information from interviews with community representatives about the attitudes of the community toward any actual or prospective branch closings.

A review of the bank's branch record should include at a minimum the following items:

- Any actions the bank has taken to minimize the impact of branch closings by trying to continue to offer services by alternate means, such as providing a way for customers to continue to obtain credit, installing ATMs or night deposit facilities, or by promoting continued productive use of the branch building.
- Any attempts the bank has made to prevent closing any branches by adjusting hours, services, facilities, finding alternative sites

suitable to community residents, or the like in an attempt to make the branch viable.

- —The bank's written plan for opening or closing its branches, if applicable. (Also review minutes of board of directors meetings for discussion of same.)
- —The bank's system to account for expenses, income and profitability of branches and the application of this system to branch closings. (Also review minutes of board of directors meetings for discussion of same.)
- —Any studies that may have been done to determine whether other financial institutions adequately serve neighborhoods where bank branches are or will be closed.

- The bank's participation, including investments, in local community development and redevelopment projects or programs.

Review written lending policy and procedural manuals and interview lending officers to ascertain whether current programs include, or if the bank has considered involvement in, programs for satisfying potential credit needs such as the following:

- —HUD's Community Development Block Grant Program.
- —Local neighborhood preservation efforts.
- —Community Development Corporations.
- —Financing for Local Development Corporations.
- —Neighborhood Housing Services.
- —Investments in, or coordination with Minority Enterprise Small Business Investment Corporations (MESBICs), or Small Business Investment Corporations (SBICs) in providing loans to business for which equity or subordinated debt is provided by MESBIC or SBIC.
- —Purchase of securities of state and local housing agencies.

- The bank's origination of residential mortgage loans, housing rehabilitation loans, home improvement loans, and small business or small farm loans within its community, or the purchase of such loans originated in its community.

Review the bank's financial statements, other appropriate records including HMDA statements, its written lending policy and procedural manuals, and interview lending personnel to ascertain whether the bank has originated or purchased such loans or has plans to do so.

- The bank's participation in governmentally-insured, guaranteed, or subsidized loan program for housing, small business or small farms.

This information may be obtained in ways similar to the ones in the assessment factor above. Examples of such government loan programs include:

- —FHA/VA/FmHA mortgage loans to members of its community or communities.
- —FHA Title I home improvement loans.
- —SBA loan guaranty programs.
- —Similar programs conducted by state or local agencies.

- The bank's ability to meet various community credit needs based on its financial condition and size, legal impediments, local economic conditions and other factors.

The financial condition of the bank may be ascertained from discussion with other examiners or review of examination work papers and reports. Small banks may not have the specialized staff or financial resources needed to participate in some loan programs.

Legal restrictions on permissible activities, interest rates, and branches may affect a bank's ability to help meet community credit needs. Adverse economic conditions caused by local or general economic difficulties may force a bank to temporarily curtail its lending activities.

Other factors may affect a bank's ability to help meet community credit needs.

- Other factors that in the Corporation's judgment reasonably bear on the extent to which the bank is helping to meet the credit needs of its entire community.

Pertinent factors may include:

- —Purchases of state and municipal bonds, secondary mortgage market securities, or such other activities when they further special purposes in the community, such as the construction or rehabilitation of low- and moderate-income housing or other neighborhood or community development, or are issued by municipalities or other local public financing units which do not have access to the capital markets.
- —Whether the bank's policies promote efforts to assist existing residents in neighborhoods

undergoing a process of reinvestment and change.

— Whether the bank offers "basic financial services" such as low cost transaction and savings accounts with low or no minimum balances, accounts for consumers who use a limited number of checks or drafts, and other accounts on which minimal charges are made for account maintenance. The marketing efforts for these types of accounts should also be evaluated.

— Any other relevant factors.

In some instances, it may prove beneficial or necessary to the assessment process to contact persons or organizations outside the bank to help determine the bank's record of meeting community credit needs and to identify unmet credit needs. The following are examples of types of outside contacts the examiner should normally make:

- Any person or organization that has specifically requested to speak to an examiner on a CRA or fair housing lending matter;
- Any person or organization that has raised in a CRA comment letter a substantial issue which requires further explanation or verification;
- A sample of persons or organizations with whom the bank has said it communicated. (This form of contact, however, should usually be made only in circumstances where the examiner determines a need to independently verify the bank's efforts to ascertain local credit needs.)
- Where there are indications of prescreening on the basis of race or sex or other disparate treatment of minorities or women, any person organization that is likely to receive complaints or other information concerning such treatment.
- Any other person or organization likely to provide valuable information concerning the credit needs of the bank's community, its efforts to ascertain those needs and make known its credit services, or its efforts to meet the credit needs of the community. Examples include local community development officials, real estate brokers, city and county officials, chambers of commerce, community action groups, local business persons and clergymen.

Initial contact may be made by telephone and suffice as adequate in some instances. An in-person interview should be conducted, however, whenever considerable information is likely to be provided, a number of people may be interviewed at the same location or relevant documentation may be made available for review. Outside contacts should be documented either in the workpapers or in the supervisory section of the Compliance Report, including the names and titles of the persons and/or organizations contacted and a brief summary of their comments regarding the bank's record of performance in the community.

9. Determine if the bank's record of performance demonstrates a recognition of its continuing and affirmative obligation to help meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operation.

10. Review the following with management:

    - The extent to which the bank is helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operation.
    - Suggestions that might better enable the bank to help meet the credit needs of its entire community.
    - Procedural violations of the regulation.
    - Deficiencies or exceptions in policies or practices.

CONSUMER COMPLAINTS

INTRODUCTION

Consumer complaints can play an important role in the supervision of bank activities as well as in policy development. They are a tool for identifying problems, for drafting desirable legislation and regulations and for protecting both users and providers of financial services.

Under section 18(f)(1) of the Federal Trade Commission Improvement Act (15 U.S.C. 57a), the FDIC was required to establish a separate division of consumer affairs to receive and take appropriate action on complaints alleging unfair or deceptive acts or practices by insured state nonmember banks.

ROLE OF THE OFFICE OF CONSUMER AFFAIRS

The Office of Consumer Affairs (OCA) is responsible for monitoring, coordinating, and evaluating the effectiveness of the processing of consumer complaints and inquiries and for recommending policies and procedures designed to efficiently and effectively resolve them. Key activities relative to the foregoing include:

- Providing assistance and advice to Regional Office staff as needed.
- Reviewing consumer complaints and inquiries handled by the Regional Offices for adequacy, consistency and timeliness of response.
- Identifying problem areas in need of additional enforcement efforts, and developing proposals for the revision of existing regulations or laws.
- Maintaining and improving as needed the computerized consumer complaint information system.
- Providing information to Congress, consumers, bankers and examiners on the complaint process.
- Coordinating efforts with other federal bank regulatory agencies.

ROLE OF THE REGIONAL OFFICE

The Regional Offices are responsible for executing policies relating to complaints of bank customers. Specifically, the Regional Office staff investigates complaints to determine their validity, decides the nature of appropriate corrective action under the circumstances and documents whether a practice or act represents an isolated case or a general condition.

GENERAL COMPLAINT-INVESTIGATIVE PROCEDURES

The following investigative procedures apply to all complaints unless otherwise specified. Since no two complaints are exactly alike, investigative procedures may vary both as to scope and sequence of the steps to be followed. Therefore, these procedures should be used as guidelines only.

Preliminary Actions

Establish the type of complaint that has been filed and how it should be processed. There are generally four types of complaints, those involving:

- An alleged violation of existing federal laws or regulations;
- An apparent misunderstanding of banking procedures or law;
- An allegation of a bank error (includes disputes); and
- Objections to or comments regarding existing policies or laws.

Some of these complaints may involve jurisdictions outside the Corporation such as state or local governments or other federal financial regulatory agencies. In these cases, the complaint should be referred to the proper agency for handling. For those complaints within the Corporation's jurisdiction, review the law, regulation, and/or rule believed to be violated. Determine whether the complaint merits an on-site investigation. In so doing, consider whether:

- The complainant indicated that the bank may be in substantial noncompliance with consumer or civil rights laws, including allegations of discrimination on a prohibited basis and/or inconsistent treatment of applications;
- Other consumer complaints of a similar nature have been received concerning the bank (see Bank Reference Report and correspondence file);
- The bank has a history of discrimination, or repeated compliance violations indicated in Compliance Reports, correspondence or from other sources.
- Purposeful, pretextural, or "effects test" discrimination was revealed in the most recent compliance examination;
- There exists any indication that a possible bank error or violation of law occurred that affects a number of other bank customers;
- The alleged banking practice cannot be verified easily by documentation or letters from bank

management and/or may require an extensive review of bank records in order to resolve.

- The accuracy and completeness of responses and documentation furnished by bank management is questionable; and
- Evidence indicates that bank management is carrying out a prohibited policy and/or practice.

It should be noted that closing cases when an accommodation to the complainant has been made does not assure protection to similarly situated consumers nor does it protect the bank from the possibility of class action suits and substantial damages. Therefore, if the bank makes an accommodation, determine whether to continue the investigation or, by a memorandum to the file, direct that specific problems or areas be looked into at the next examination. In deciding this, consider whether the allegation, although resolved for that consumer, may have involved a pattern or practice involving other customers.

If a decision is made not to conduct an on-site investigation at the time of complaint, a letter should be written to the bank setting forth details of the complaint and asking for the bank's position along with relevant documentation. The letter should establish a deadline (within 30 days) for the bank's response. Follow-up should be made promptly (within 15 days) if the bank response is delayed.

A bank which is the subject of a complaint should be contacted in most cases because consumers frequently do not express fully and clearly their problems and contacting the bank may provide additional information. Moreover, banks should be given an opportunity to correct any operating deficiencies and to rectify voluntarily any problem.

Review the statistical complaint sheet (Bank Reference Report) and/or complaint file to determine if any other complaints of the same type have been filed previously against the bank and if so, how they were resolved. Note the name of the person at the bank who was contacted and review any letter the bank may have written regarding the complaint.

ONSITE INVESTIGATIONS

Interviewing the Complainant

The complainant should be the first person contacted, either by phone or in person, unless doing so would unduly delay the investigation. In many cases, this will yield information not provided in the initial correspondence. During the contact:

- Obtain full name, address and telephone number of the complainant. Identify the sex, age, race, etc., if that information is pertinent to the investigation.
- Ensure that the complaint is still outstanding.
- Determine specifically what the complainant desires in order to resolve the complaint (i.e., damages, an apology, the type of credit, etc.).
- Obtain the names of all persons involved in the complaint, including bank officers.
- Do not discuss the merits of the complaint or the status of the investigation. Indicate that the Regional Office will be responding to the complaint after all the facts have been obtained.

Interviewing Bank Personnel

Fact finding interviews of bank personnel should be held individually. The names and titles of all parties involved in the complaint should be obtained. An effort should be made to ascertain how the bank desires to resolve the complaint.

Bank procedures and documentation should be reviewed to determine whether the allegation is true and whether it is an isolated case or a recurring situation. Any defenses or explanations offered by bank officials should be analyzed. Obtain copies of any written instructions to employees with respect to practices and procedures concerning the complaint. Establish unwritten instructions through the interview process. Copies of any other documentation pertinent to the complaint (i.e., ledgers, tickets, receipts, coupon books, etc.) should be included in the workpapers. If necessary, apprise the bank of its responsibilities and those of the Corporation and of the Corporation's powers to enforce regulations.

Exit Interviewing

At the conclusion of the investigation an interview should be held with the president or other responsible executive officer to discuss findings regarding violations and/or procedural deficiencies. Recommendations that the bank take corrective action on the complaint should not be made at this time unless instructed to do so by the Regional Office. The final determination as to the merits of the case will be made by the Regional Office after all facts have been reviewed and analyzed.

Investigative Report

The examiner should write a report presenting the facts and information in a clear, objective manner. The report, in memorandum form, should:

- Be dated and written in the third person.
- Summarize the facts in chronological order.

- Indicate the parties involved.
- Detail the precise claim(s) of the complainant.
- Detail the resolution desired by the complainant.
- Detail information or material gained which supports the claim(s), including management's expressed policies and procedures for the relevant subject area and whether bank records (deposit and loan account files, correspondence files, etc.) reflect practices which tend to support management or the complainant.
- Detail all violations noted relevant to the complaint. Indicate whether infractions are the result of errors or mistakes, as distinguished from deliberate violations.
- Indicate bank management's response to the claim(s), together with any supporting documentation or other evidence provided by management.
- Summarize the above facts, develop conclusions based on the evidence as to what took place, whether the bank appears to have acted improperly or unlawfully, and how the complaint could or should be resolved. All allegations and defenses should be reported and labeled as such.
- The examiner should comment in the summary section on whether the complaint represents an isolated case or a pattern or practice.
- All recommendations for corrective action should be fully supported and referred to the Regional Office for decision (see the discussion to follow on discrimination complaints and also, review the Corporation's ECOA/FHA Enforcement Policy Statement for guidance).
- The examiner should provide a breakdown of hours expended on the investigation including travel performed during working hours.

Instances of discrimination which are not the subject of the complaint being investigated should be reported to the Regional Director by separate memorandum. The investigation workpapers, together with any other supporting documentation, as well as a copy of the investigation report, should be retained on file at the Regional Office (also, the Regional Office should have on file all complaints so that examiners may use them to brief themselves before beginning any subsequent examination or investigation).

A letter will be sent from the Regional Office to the complainant explaining the findings of the investigation, the corrective action, if any, the Corporation will require the bank to undertake, and any alternatives (e.g., civil suit) that may be available to the complainant (whether or not corrective action is required).

A letter will be sent from the Regional Office to the bank indicating the findings and required corrective action. The bank may receive a copy of the letter sent to the complainant. Any corrective actions required should normally be accomplished within 30 days.

As a general rule, copies of the investigation report and the complaint will be released to the complainant or to the bank upon request. Under the Freedom of Information Act (FOIA), some or all of the information in the complaint file may be made available to the public without identifying the complainant.

COMPLAINT PROCESSING GUIDELINES

The following time limits should be followed in responding to the complaints:

- Complaints should be acknowledged within 15 business days after receipt of the correspondence in the Regional Office.
- Inquiries, comments, or objections should be answered or the information provided within 15 business days after receipt in the Regional Office.
- Complaints not involving an on-site investigation should be fully processed and responded to within 30 business days after receipt in the Regional Office.
- Complaints involving an on-site investigation should be resolved within 45 business days after receipt in the Regional Office. Exceptions to this time limitation caused by staffing, scheduling, or other problems should be documented by a memorandum to the file with a copy to the OCA.

All written consumer complaints and inquiries, including those directed elsewhere with a blind copy to the Corporation, should be responded to in writing in order to acknowledge receipt of the complaint, explain the Corporation's jurisdiction (or lack thereof with appropriate referral), or offer additional information or assistance as necessary. If the addressee is a bank and the Corporation receives a blind copy, the correspondence should be acknowledged to the consumer as having been received. In that acknowledgement, the consumer should be informed after receipt of the bank's response to contact the Corporation directly for assistance if he or she believes the problem is not resolved.

The Regional Office has the option in high complaint volume situations of explaining in the acknowledgement letter to the consumer that the complaint or inquiry has been forwarded to the bank and that the bank will respond directly to the consumer. The consumer should be informed after receipt of the bank's response to contact the Corporation directly for assistance if he or she believes the problem is not resolved.

The Regional Office should write a separate letter to the bank forwarding the consumer's correspondence (a number of consumer complaints can be enclosed with this letter) and instruct the bank to respond directly to the consumer(s) with a copy to the Regional Office in order to review and ascertain whether appropriate action has been taken. This arrangement should be negotiated and agreed to by the bank. The Regional Office will review these copies to ensure all issues have been addressed by the bank in its response to the consumer. The Regional Office will forward copies of the bank's response to the Washington Office (OCA) to close the Consumer Complaint and Inquiry System file.

Under the Privacy Act, consumers have a right to a copy of anything in their file. Therefore, if a consumer requests a copy of the investigation report relative to his or her complaint, an unexpurgated copy (except for names of other consumers) may be provided upon request to the Corporation's Executive Secretary in Washington, D.C.

A complaint file should be closed when it becomes apparent that the Corporation can or should do nothing more under the circumstances. The consumer should be informed that the matter is considered closed and that the case will not be reopened unless new material is presented. If the consumer continues to write without presenting any new information, he or she should be notified that further correspondence will not be answered and this should be documented in the file.

DOCUMENTATION OF COMPLAINTS

Written complaints which involve a Corporation supervised bank and which are received by the OCA generally will be referred to the Regions for action by copy of an acknowledgment letter to the consumer. Written inquiries and certain complaints not requiring on-site investigations will be answered directly by the OCA.

The original of each incoming consumer complaint or inquiry received in the Region should be sent to the OCA. Copies of all acknowledgments, bank correspondence, final responses, and investigation reports or other documentation prepared or collected by a Regional Office should also be sent weekly to the OCA. If initial contact with the bank is by telephone, the date should be noted in the file. The information is needed by the OCA to update the computerized complaint tracking system, to review the progress of various cases, and to evaluate the adequacy and consistency of both complaint resolutions and responses to consumers.

If it is determined that no letter response is needed, note clearly on the face of the incoming letter or in a memorandum to the file why no written response was made. Also note the date on which the case was closed by the Regional Office. Correspondence referred by a member of Congress, the Chairman's Office or the Director's Office should be processed expeditiously. Telephone and walk-in complaints and inquiries should continue to be reported on the Consumer Telephone and Visitation Log in accordance with the related instructions. Normally, complaints should be in writing; however, oral complaints should be followed up when the complainant is unable to write. As with any complaint, the extent of the inquiry into or investigation of an oral consumer complaint, and the methods employed, may vary depending on a number of factors, e.g., the apparent nature and substance of the complaint, its plausibility, the specifics provided and any previous experience with the complainant.

Copies of any correspondence relating to a complaint originally logged by telephone should be sent to the OCA in the same manner as other consumer correspondence. Efforts to resolve telephone complaints should be described on the Telephone Log or by memorandum to the file in cases where formal correspondence or documentation is not produced. If a decision is made not to investigate and resolve an oral complaint, it should be documented either on the Telephone Log or in a memorandum to the file. Copies of these entries to the Telephone Logs and memoranda should be sent to the OCA.

COMPLAINTS ALLEGING GENERAL CREDIT DISCRIMINATION

Complaints alleging illegal credit discrimination are frequent. The Equal Credit Opportunity Act (ECOA) is the federal statute which relates directly to discriminatory lending practices by banks (the Fair Housing Act will be discussed below in this section). Because the ECOA is a civil rights statute as well as a consumer protection law, the law is to be interpreted broadly.

The area of discriminatory practices is broad and varied. The following four general classifications of discriminatory conduct are useful guides in analyzing lending practices:

- Purposeful discrimination (when motivated by prohibited bases considerations). This includes:

- — Overt (when a prohibited basis is openly considered);
- — Pretextual (when there are asserted nondiscriminatory reasons to justify discriminatory acts);
- Subjective standards which are vague and undefined may produce otherwise unexplained discriminatory results;
- Present effects of past practices (when loan criteria do not take into account the discriminatory effects of past practices); and
- The "effects test" (when there is a statistical showing of a disproportionate impact on a protected group but where there was no discriminatory motivation of any kind).

A lending practice may involve more than one of the above types of discrimination. When presented in the investigative report, findings of discrimination should use these classifications.

Investigative Procedures (General)

Review the General Complaint Investigative Procedures and include the following:

- Determine the bank's pertinent policies (current as well as those in effect at the time the event took place). The accuracy of this information is particularly important when the bank's policies are not in writing and need to be verified with members of the staff. With complaints involving a credit scoring system, obtain a complete description of the system, a copy of any written guidelines and determine how the system is actually used, e.g., when overrides are allowed.
- Compare the stated and applied standards for offering credit, including all factors taken into account in determining whether a given applicant is eligible for a loan. Determine if the bank makes exceptions to these standards, how the exceptions are applied and if the complainant would qualify based on these exceptions.
- Determine if the bank personnel involved in the alleged discriminatory act interpret and apply these standards as intended by bank management.
- Determine whether and in what form any of the following factors were taken into account, either directly or indirectly, in considering the credit application: the applicant's race, color, religion, national origin, sex, marital status, age, receipt of public assistance funds, or good faith exercise of rights under the Consumer Credit Protection Act.
- Verify the lender's policy by comparing accepted and rejected applications. In cases where a complainant alleges discrimination on a prohibited basis through the application of lending requirements, review the files of accepted applications to look for applicants who were accepted with that same negative lending factor present.
- Sampling and comparison procedures are especially important in investigating credit discrimination. A sample of accepted and rejected applications can be drawn and compared to the complainant's situation. The usual procedure in credit discrimination analysis would require that the loan files and treatment of certain groups be compared against the files and treatment of other groups. Because section 202.5(d)(3) and (5) of Equal Credit Opportunity Regulation B prohibits a creditor from requesting the sex, race, color, religion, or national origin of the applicant, these groupings are almost impossible to identify. However, individual women (identified on the basis of first names) can usually be compared to married couples. Identify exceptions made for some applicants to policies and determine why a similar exception was not made for the complainant or for others similarly rejected.

Determine differences in treatment based on actual standards or practices versus the stated ones. Utilize the Home Loan Worksheet in Section II-B, as applicable, to document this comparative analysis.

The investigation report should reflect any violations in the following areas, which are considered especially serious and will usually be subject to retrospective corrective actions:

- Discouraging applicants on a prohibited basis.
- Using credit criteria in a discriminatory manner in evaluating applications.
- Imposing disparate terms on a prohibited basis.
- Failing to furnish separate credit histories.
- Failing to provide adequate notices of adverse action.

The bank will usually be required to correct the effects of all such violations discovered and take action to ensure that they do not recur. Situations where discriminatory patterns and practices exist will usually necessitate formal enforcement actions. Specific corrective actions should be tailored to the cases involved.

In any case where a complaint alleging discrimination on a prohibited basis does not result in an on-site investigation, a memorandum to the file should explain the action, with a copy of the memorandum forwarded to the OCA.

COMPLAINTS ALLEGING HOUSING DISCRIMINATION

Complaints alleging illegal mortgage lending discrimination vary in volume based on mortgage market activity. Four federal statutes relate to discriminatory mortgage lending practices by financial institutions: the Fair Housing Act (FHA) which is Title VIII of the Civil Rights Act of 1968, the Equal Credit Opportunity Act (ECOA), the Home Mortgage Disclosure Act (HMDA), and the Community Reinvestment Act (CRA). The CRA does not speak directly to discrimination but is concerned with geographical disinvestment which may occur on the basis of, or especially affect in an adverse manner, persons in protected categories. The issue of mortgage redlining underlies both the CRA and the HMDA.

The ECOA and section 805 of the FHA apply to banks as creditors (creditors are those who regularly participate in the decision of whether or not to extend credit). The HMDA applies to banks with more than $10 million in assets which have a main or branch office located within an MSA and which make federally related mortgage loans. The CRA applies to all financial institutions regulated by three federal bank supervisory agencies and the Federal Home Loan Bank Board.

Examples of bank practices which constitute unlawful discrimination in mortgage lending include, but are not limited to, the following:

- Discouraging a prospective borrower on a prohibited basis, at an initial or early stage of negotiation.
- Discounting or disregarding the income of a working wife or unmarried woman when a similarly situated man's income would not be discounted.
- Subjecting a female applicant to a different or more extensive credit check than that usually required for a male applicant.
- Treating unmarried working mothers differently than unmarried working fathers.
- Requiring female applicants, but not male applicants, to obtain a cosigner.
- Basing any aspect of a lending decision, in whole or in part, on the racial or ethnic composition of the area where the property is located.
- Accepting a loan application, but only on terms sufficiently unfavorable (on a prohibited basis) to cause the applicant to withdraw the application.

Examples of bank practices which may serve as indicators leading to the identification of Fair Housing violations include:

- A lack of applications from protected group members and/or from census tracts and/or neighborhoods with a significant representation of protected group members.
- A disproportionate denial of loan requests from members of a protected group.
- Bank branches located in areas with high percentages of protected group members which do not have mortgage loan applications available or do not take applications.
- Unusual delays in acting on standing applicationssubmitted by protected group members.
- HMDA data or log sheet data inadequately collected or not collected at all.
- Ultra-restrictive underwriting/appraisal policies or standards such as large lot requirements, garage(s) required, no older building policy, high minimum loan amounts, large minimum square footage, unusually short maturities, previous homeownership required, low maximum loan-to-value ratio.
- Most real estate applications referred by a few brokers or agents; selective contact with real estate brokers.
- Advertisements directed at majority members only, new houses only, upper-middle class only.
- None or few minorities represented among the creditor's staff even though minorities account for a significant portion of the local community.
- An appraisal practice such as the down-valuing of older buildings (versus condition of building).
- Underwriting and appraisal policies or standards which are unavailable to the public or which appear to be selectively applied on a prohibited basis.
- Race, sex, or another protected category appear to have been used as a factor in determining the risk of a loan and in determining the terms and conditions.
- Certain geographic areas restricted to FHA loans.
- Certain census tracts and neighborhoods appear to be granted less favorable loan terms because of protected group residents such as higher downpayments, higher interest rates, and shorter loan maturities.

Investigative Procedures (Housing)

The same complaint of credit discrimination may violate the FHA and ECOA. For processing purposes, the following distinctions apply:

- A mortgage financing complaint is processed as an ECOA complaint when the complainant alleges discrimination based on marital status, age, source of income (i.e., public assistance) or because an applicant has in good faith exercised any right under the Consumer Credit Protection Act.
- A mortgage financing complaint is processed as a Fair Housing complaint when the complainant alleges discrimination based on race, color, religion, sex or national origin.

When a Fair Housing Complaint is received concerning a bank supervised by the Corporation, the Regional Office should send a copy of the complaint to the OCA to be forwarded to HUD in accordance with an interagency agreement ("Memorandum of Understanding Regarding Interchange of Information Concerning Complaints Involving Discrimination in Financing") with the Department of Housing and Urban Development dated September 2, 1976. Any complaints forwarded to the OCA by HUD under this agreement are forwarded to the appropriate Regional Office for information purposes, unless otherwise specified.

For almost all Fair Housing complaints, an on-site investigation is standard operating procedure. There is always an advisement of legal rights in the acknowledging correspondence to the consumer. (A suggested format can be found following the case study at the end of this section.) Also, the examiner should interview the complainant.

Under the General Complaint Investigative Procedures, substitute the following steps for those following the interview with the complainant. (Note: These investigation procedures are comprehensive in scope and the implementation of individual items or parts is to be determined by the types of information needed to answer the question(s) raised in the complaint.)

Develop the following information regarding the complainant's initial contact with the bank:

- The reason(s) the complainant contacted the bank.
- The approximate date of the initial contact and the method of contact (telephone, mail or in person).
- The person the complainant contacted at the bank. If the person's identity is not known, ascertain his or her title and a description, if possible.
- The information initially requested by the bank (location of property, age, employment characteristics, etc.).
- The information provided by the complainant, either voluntarily or as a result of a specific request. Ascertain all details of the complainant's response, including any additional questions asked, any indications that not all of the wife's income would be considered or that the wife's income would be considered only in certain circumstances. Any such specific indications should be noted.

Obtain details on the nature of the complainant's loan request, including location of the property, purchase price, down-payment available, loan amount, interest rate, duration and type of loan (conventional, FHA or VA).

Inquire whether the complainant believes that he or she was discouraged by the bank in filing an application, obtaining a loan on the terms requested or in the area where the property is located. Obtain all details. If there were witnesses to any of the dealings with the bank, obtain their names, addresses and phone numbers, if possible.

Application Analysis

Inquire whether the complainant ultimately submitted a formal application to the bank. If not, ascertain the reason. Determine if an application was subsequently submitted to another institution and its disposition as well as full details of any subsequent dealings with the bank.

If the complainant did submit a written loan application to the bank, obtain details of the type, amount and duration requested, if different from the complainant's initial request. Ascertain when the application was filed and with whom the complainant dealt. Determine whether the complainant had a personal interview with a bank representative and, if so, the identity of that representative. If the loan was approved, declined, offered on other items or withdrawn, obtain all details (i.e., why it was withdrawn, other terms offered and all reasons given, in writing or orally, etc.). If the complainant tried to obtain additional information or had other contact thereafter, ascertain exactly what happened. Obtain copies of all correspondence and documents relating to the loan application which the complainant can provide. Determine whether the complainant believes that the reason given by the bank for rejecting the application was the actual reason and, if not, what he or she believes the actual reason was and the basis for that belief.

If the bank's rejection was based on insufficient income or credit reasons, obtain the following information:

- Total gross income at time of application (both spouses);
- Sources of income (including child support and alimony, part-time jobs, etc.);
- Total amount of debts other than the proposed mortgage debt;
- Total monthly payments on debts (including child support and alimony);
- Bankruptcies, delinquencies, or other adverse credit history which might have been cause for rejection;
- Marital status of applicants, age of applicants, number of children and their ages; and
- Employment history and number of years in current employment.

If the complainant believes the bank's rejection was based on sex discrimination, ascertain if the application was joint, whether both spouses were present at the time of application and whether both participated in providing information to the bank. Determine who filled out the application form and whether it was assumed by the bank that the husband was to be the "borrower" and the wife the "co-borrower." Inquire whether there was any difference between the bank's questions concerning the employment of the husband and those concerning the employment of the wife and, if so, what the difference was. Determine whether either spouse had any plans to change employment in the future and whether the husband was asked about his plans for future employment. If the wife was asked about her plans for future employment, inquire whether more information was requested concerning the wife's plans than the husband's and whether there was any suggestion that the wife would be likely to stop working in the future. Determine the number and ages of any children the complainants had at the time of the application and any questions the bank asked about their plans to have children in the future, whether they were practicing birth control or the kind of birth control they practiced. If such questions were asked, what reason did the bank give for requesting the information. Inquire also whether the bank required any assurances that the complainants were not planning to have children as a prerequisite to counting the wife's income and, if so, what assurances were required. Ask whether the bank indicated to the complainants that there was a possibility that not all of the wife's income would be counted in determining their eligibility for the loan. If so, what was said and who said it. Ascertain whether there was any indication that the husband's income would be considered first, and the wife's income would be considered only if his was insufficient to qualify alone. If so, obtain details. To the complainant's knowledge, did the bank contact both the husband's and the wife's employers to verify their employment and when were these contacts made.

Bank Visitation

The examiner should obtain a clear and specific statement of the bank's lending policy for the type of loan requested by the complainant at the time the loan was made. The accuracy of this information is particularly important when the bank's loan policies are not in writing.

Initially, the bank should be provided with a copy of the written complaint. In addition, all individuals contacted at the bank and referred to either in the examiner's workpapers or investigation report should be identified by name, title, race and sex.

Depending on the nature of the complaint, one or more of the following subject areas should be researched:

- Documentation

  Obtain copies of any manual, book or compilation of memoranda or minutes (including memos to employees) describing or containing the bank's loan policies pertaining to the different types of loan requests. This might include underwriting criteria, standards on evaluating income, directives as to current interest rates, loan-to-value ratios, etc. If there have been changes in the past two years, obtain a copy of the previous version.

  If the bank states that no such compilation exists determine how employees, such as branch managers, know what information to give applicants about present policy or what standards to apply to applications. If the bank states that this information is communicated orally in meetings, determine if minutes were taken. Obtain copies of all written instructions to employees with respect to lending policies, practices and procedures. Obtain copies of the following forms presently used or in use at the time of the complainant's loan request:

  — All loan application forms.

  — Appraisal forms.

  — All worksheets for computing and evaluating credit information.

  — Bank memoranda concerning current mortgage terms available (e.g., interest rates, loan-to value ratios, etc.). If not available, ascertain if the information can be abstracted from other sources such as board minutes or written loan policy statements.

- Any written material prepared for the use and information of builders or brokers who refer applicants to the bank.

- General Loan Policies

Obtain the following information on loan terms:

- Maximum and minimum loan amounts and how these ranges are determined (e.g., by federal law, regulation, internal policy, or a combination) and also what circumstances would justify a deviation from these limits.
- Maximum and minimum interest rates and what circumstances would justify a deviation from these limits.
- The person or group that officially sets the maximum and minimum limitations described above.

Obtain a description of all limitations regarding the property and its location which are presently observed or which were observed at the time of the complainant's loan request, and the relationship of such limitations to the loan terms and conditions. These can include:

- The age of the property. Is there a limit on the age of property that will qualify for a conventional loan? Is this chronological age effective age, or remaining economic life? Are there any circumstances under which the age limits would not be observed? Does the age of the property dictate the duration of the loan? If so, on what scale? Are there any exceptions to this? Obtain a complete description of all circumstances in which age of property affects a loan application.
- Style or size of property.
- Crime rate or vandalism rate in an area. How is this measured or determined?
- Economic level of residents in an area. How is this measured or determined?
- The age or age range of other properties in the neighborhood where the property is located.
- The value range of other properties in the neighborhood where the property is located.
- The predominant racial or ethnic composition in the neighborhood where the property is located. is this composition changing? The percentage of the neighborhood that is developed.

Obtain a complete description of all factors affecting the neighborhood where a property is located which can have a bearing on the approval of a loan or its terms. Ascertain in particular whether racial or ethnic composition is ever a factor and, if so, how is this taken into account?

Obtain a list of any specific areas where the bank prefers to make loans or has made the majority of loans in the past two years. Obtain a description of these areas (housing and population characteristics, e.g., new communities rather than older ones).

If there are areas, streets, communities, or neighborhoods where the bank will not make loans, obtain a description of the boundaries of such areas and determine why no loans are made there. If exceptions have been made, determine how many, when and whether there is a high delinquency or default rate on such loans. Also determine the bank's estimate of the number of applications, per month, from such areas. If the number is low, determine why the bank believes more applications do not come from these areas.

If there are any areas, streets, communities, or neighborhoods where the bank will only make FHA or VA loans, obtain a description of the boundaries of these areas and the bank's reasons for making only FHA and VA loans. Also determine whether the bank has ever made conventional loans in the area and, if so, how many, when and whether there was a higher delinquency or default rate on such loans. Have the bank estimate the number of applications for conventional loans, per month, from such areas. If the number is low, determine why the bank believes it to be low.

If there are areas, streets, communities or neighborhoods which, for any reason, the bank considers to be high risk areas for lending but in which it will make conventional loans on a high down-payment, low loan-to-value ratio basis at higher than market rates or for a shorter duration, obtain a complete description of the boundaries of such areas and why the area is considered high risk, how that risk is measured and how terms are fixed for loans in such areas. Also determine the bank's estimate of the number of applications for loans, per month from such areas. If the number is low, determine the bank's opinion of why it is low.

Determine whether the bank has a policy against originating or processing FHA loans and, if so, why. Ascertain whether there was ever a time during which such loans were made and, if so, when and why the policy changed. If there are any areas where the bank will not originate FHA loans, obtain complete details.

Determine whether at any time during the past five years the bank was "out of the market" for home mortgage loans generally or in a particular area. If so, determine the dates of such a condition and the reason for it. If any home loans were being made at that time, determine to whom they were made.

Determine whether the bank gives or has given any preference to depositors in granting loans and, if so, how the preference operates.

Determine whether the bank has maintained any ongoing relationship with builders or brokers who refer single-family home loan applicants to the bank. If so, obtain a description of the relationship, the name and address of each broker or builder and the name of the contact person in such organization.

Determine how salespeople in these organizations are advised of the bank's requirements or terms. If any material is in writing, obtain copies. Determine the bank's estimate of the number of single-family home loans which are the result of existing bank relationships, "walk-ins," the percentage referred by brokers, the percentage referred by builders and the percentage referred by other sources.

Determine if the bank has been the subject of a complaint of discrimination in lending or employment on the basis of race, age, color, religion, sex or national origin within the past two years. If so, obtain all details of such complaint, the agency which handled it, the identity of complainant and the resolution. Obtain a copy of all documents and correspondence in the bank's possession with respect to the complaint (if not already available in the Regional Office files).

- Analysis of Application Procedures

  Obtain the following information with respect to loan applications:

  —The place(s) where application forms can be obtained and where they can be submitted.

  —The existence of any application appraisal fees, how much they are, when they are paid and whether they are always paid, and whether they are retained if the loan is declined.

  —The name of any persons authorized to review an individual's financial data or property characteristics to determine eligibility prior to an application being submitted (prescreening), how the procedure operates and whether any record is kept of applications not ultimately submitted. Ascertain whether the practice occurs even though not formall authorized.

  —Information given to prospective applicants by phone and whether any prequalification or prescreening is done by phone.

  —Information requested of an inquirer who telephones for information. In particular, determine whether the property address is requested and why. Inquire whether persons are ever told on the phone that loans are not being made in certain areas and, if so, under what circumstances this would occur.

  —After an application is submitted, where does it go (i.e., is it forwarded to a central loan department or do branches process them).

  —The checks and verifications performed on information reported on the application.

  —When the appraisal is ordered and under what circumstances an appraisal would not be ordered.

  —After all information is verified and the appraisal returned, who then reviews the file. If any information cannot be verified or is unfavorable, ascertain whether the application can be rejected at this stage and, if so, who has authority to make such a rejection and what records are kept.

  —If information on the application is verified and the appraisal supports the loan request, who is authorized to accept or reject the application (a loan committee, loan officer, board of directors).

  —If an application is rejected, how long is it retained.

  —How information on approved loans is retrievable.

  —How loan jackets are organized and filed.

  —If a separate file of appraisals is kept, how it is organized.

  —Whether applicants fill out their own applications or whether it is done by the bank.

  —Whether applicants are asked to sign a blank application so that information may be typed in later.

- Analysis of Underwriting Policies

  Obtain a description of all factors which go into the decision that an applicant is qualified, the property is eligible and the specific terms and conditions of each loan. These factors may include the following:

  - Sufficiency of income. What loan-to-value, mortgage payment to income or total payments to income ratios or formula are used and why were these ratios adopted? Under what circumstances might these ratios be varied and a loan made even though the income does not meet the test?
  - Viability, stability or reliability of income and income sources. How are these elements measured, what factors are looked for, and do they vary according to the applicant's profession or social status? Ascertain in particular whether any types or sources of income are discounted or not counted (e.g., part-time income, bonuses, commissions, income from jobs held less than two years).
  - Total qualified income. Is this income calculated on the basis of one spouse's income or both spouses' incomes? If any one income is used, ascertain which one, why and when the other spouse's income would be included. Determine whether any preference is given to loans based on only one, as opposed to two incomes.

  Obtain a description of the bank's policy with respect to:

  - The income of working women (are there any circumstances under which it might be discounted or disregarded?)
  - Loans to unmarried women with or without children.
  - Inclusion of alimony or child support as viable income.
  - Viability of income for women in childbearing years.
  - The ability of a woman to obtain a loan in her own name and any co-signer requirement.
  - Credit scoring devices. If used, obtain a complete description and a copy of any written guidelines.
  - Credit history. Ascertain any factors which would disqualify an applicant (i.e., bankruptcy, prior foreclosure, late payments).
  - Property characteristics. Determine what factors go into the determination that a property is eligible or ineligible for a loan. Ascertain whether the appraiser includes comments on the future predictable value of a property or an area.
  - Loan-to-value (LTV) ratio. Ascertain the standards set by the bank if the LTV ratio applied for by the customer is considered too high. Obtain full details.
  - Risk. If a loan is believed to contain more than normal risk, determine whether it will be rejected or whether there are circumstances under which it will be made but on terms which reflect the additional risk. Ascertain who makes the determination and how the risk is measured objectively. In particular, what factors go into the decision (i.e., how are the LTV and total payments-to-income (TPI) ratios set, what standards are used to establish the durations, how is the interest rate set and how are "points" arrived at). For a loan that is accepted and not considered to involve a greater than normal risk, ascertain how the rate, term, LTV, mortgage payments-to-income (MPI), TPI and points are arrived at. In particular, who fixes them and what standards are followed. For example, with MPI, is there consistency in the application of the bank's policy? Are utility costs, taxes, insurance, etc., always included/excluded? Similarly, with TPI, are taxes, insurance, utility, and other costs always included/excluded?

  Determine if the policy with respect to any of the above items was different from present policy at any time within the past two years. If so obtain full details of prior policy, when and why a change was made and how the change was communicated to employees.

  Determine whether employees are given any instruction in the areas of civil rights or nondiscrimination in lending practices. If so, obtain all details, including copies of any written material.

- Analysis of Lending Patterns

  For those banks not subject to the HMDA, determine whether the bank can provide a list of mortgage loans by address or total number broken down by census tract or zip code. Obtain this breakdown for mortgages made in the past two years, if possible. (With respect to larger institutions this request may be modified to obtain at least a six-month sample.)

Determine the bank's estimate (if more precise data is not available) of racial and ethnic composition of its depositors and its mortgage loan customers. Complete a Log Analysis Worksheet.

Examine a sample of accepted and rejected mortgage applications for the period of time during which the complainant's application was submitted. Review and take notes on the following documents from the files of such loans: application, appraisal, worksheets, and any documents that list the amount of the loan made, interest rate, maturity, points, and date of approval. Complete a Home Loan Worksheet (HLW) for the sample. A sample Worksheet is at the end of the Fair Housing section.

Look on the appraisal form under "neighborhood data" to determine whether any racial notation or code is used. If any racial notation or code other than those required for recordkeeping purposes by the Fair Housing regulation is observed, ascertain why it is kept and how it is used.

Note whether any bank worksheet indicates that the income of a working wife was discounted or not included. Compare the figures with those entered on the application and employment verification forms. Combined incomes of both spouses must be considered in TPI and MPI computations.

Identify any applications (including the complainant's) which were rejected but which should have been accepted based on actual or articulated policies. Terms and conditions should be examined as well.

Determine the percentage (or approximate percentage or dollar volume) of home loans made in the past year which have been sold to other investors or in the secondary market. Identify the buyers and determine how loans are selected to be included in the packages to be sold (e.g., are only FHA loans sold, or loans in certain areas, or with certain characteristics). Determine if this is a greater or lesser amount than sold in previous years and the reasons for any change.

Determine whether, at any time in the past two years, the institution has had more funds available than required by qualified applicants. Identify any such time periods and determine how the funds were invested.

Determine the percentage (or approximate percentage or dollar volume) of home loans made in the past year which, rather than being originated by the bank, were purchased from other sources. Determine the identity of the other sources and the general location of the loans. Determine if this is a greater or lesser amount than purchased in previous years and the reason for the change.

- Analysis of Collection Procedures

Determine whether the race, ethnic origin or sex of the borrower is ever a factor in determining what collection steps will be undertaken. If so, obtain all details.

Determine the number of foreclosed home loans involving protected group applicants for the past two years and what percentage this is of the total mortgage portfolio. Determine the number of delinquent home loans involving protected group applicants in each year in the past two years and what percentage this is of the total mortgage portfolio. Analyze the bank's delinquencies or foreclosures from a protected group point of view to determine those factors that may have caused or contributed to the delinquency or foreclosure. Obtain all details, including copies of any written analysis.

Determine which home loans foreclosed or litigated in the past two years.

Determine the bank's policy with respect to collection and all steps taken in the collection process, including:

—Actions by the borrower which place the loan in a delinquent status or in default (e.g., one month in arrears, two months in arrears, etc.);

—Steps initially taken in these circumstances;

—Follow-up steps taken, and when;

—Circumstances under which foreclosure is instituted;

—Circumstances under which forebearance is exercised; and

—Factors that would cause the above schedule to be accelerated or decelerated.

Determine all factors which would cause a variation in the collection process (e.g., does it vary on the basis of the property's location). Obtain sample copies of collection letters and an indication of when they are used. Examine a sample of collection files or cards to determine if any bear racial or ethnic notatation or code.

OTHER SOURCES OF INFORMATION

Appraisers, real estate brokers, consumer groups, and other complainants represent additional sources of information the examiner may wish to pursue in the investigation, depending on the nature of the complaint and Regional Office concurrence.

Analysis of Appraisal Policies and Procedures

Appraisers may be bank employees or work independently on a contract basis. If the bank uses independent appraisers, contact the appraisal company and interview those persons who conduct appraisalsor did appraisals for the bank at the time of the complainant's loan request. If the appraisers are bank employees, interview all appraisers who were employed in that capacity at the time of the complainant's loan request. Obtain the following information for business conducted during the past two years:

- Name, address, race or ethnic origin, sex, employer's name and dates of employment.
- Nature of the appraiser's training, professional designation or affiliation, and years of experience.
- Approximate number of single-family homes appraised by the individual per year (or per month or week). If the appraiser works for an independent fee company, determine the approximate number done by the company and also the name and address of every lender for which single-family home appraisals were done in the past year.
- A sample copy of all forms presently in use or used within the past two years for the appraisal of single-family dwellings and which forms are or were used by or for the bank.
- Whether the racial or ethnic composition of an area is ever a factor in determining fair market value, neighborhood analysis, future value or loan risk. If so, obtain all details of the way in which these factors are affected by race or nationality
- Determine whether a pattern of underappraisals related to prohibited factors exist. Does a gap exist between appraised value and price for minority areas more frequently than for non-minority areas?
- The way in which the racial or ethnic composition of an area is reflected on the appraisal report or is reported to the bank and why it is reported.
- Whether any person associated with the bank has ever inquired about the racial composition of an area. If so, obtain all details, including names, dates and reasons for inquiry.
- Whether the appraiser has ever had any discussions, correspondence, or instruction from his superiors or from the bank with respect to a particular appraisal or appraising in general for an area which is integrated, integrating or predominately nonwhite. Obtain all details, including what was said, by whom, when, and in what manner directives where implemented.
- Whether the appraiser is aware of any map or list used presently, or within the last two years, by appraisers on behalf of the bank which demarcates geographic areas on any of the following bases:

  —Racial or ethnic composition;

  —Income level of residents;

  —Changing value levels;

  —Age range of properties;

  —Value range of properties;

  —Loan or no loan areas;

  —High or low risk;

  —Crime rate; or

  —Other similar category.

  If so, obtain all details, including how the map or list is used, why it is no longer used (if that is the case), who maintains it, and how areas are determined to belong in one or more categories. Determine where the map or list is kept and a description of each area demarcated thereon. If possible, obtain a copy of the list or map and all documents related to its use.
- The appraiser's operational definition of economic obsolescence and how this is measured. (Note: Standard appraisal texts in the past have cited the presence of "inharmonious racial groups" as a case of economic obsolescence, which leads to depreciation on the basis of race.)
- Whether, in the appraiser's professional judgment, economic obsolescence can be caused by infiltration of inharmonious groups. Determine what is meant by "inharmonious groups" and whether this includes racial groups. Determine how the economic obsolescence from such infiltration is measured or measurable. Determine whether the appraiser applies the concept of "infiltration," and if so, how.
- Determine what the appraiser construes "homogeneous" area to mean and whether this definition includes racial or ethnic homogeneity. Determine what specific areas the appraiser believes have declined in value due to the

presence of non-homogeneous people. If, in the appraiser's judgment, the presence of Black or Spanish persons is an "adverse influence" in a neighborhood, obtain all details. If the appraiser ever includes comments about the values or future of a neighborhood in an appraisal report to the bank, determine why this is done.

Contact with Real Estate Brokers

A large number of applications for loans are forwarded to banks by real estate brokers. Accordingly, local area brokers are often aware of the general loan policy of lenders and whether these policies are nondiscriminatory. For "racial redlining" complaints, the brokers most likely to have relevant information are those who deal in racially integrated or predominantly Black areas. In some respects, nonwhite brokers and agents may be the most helpful.

To conduct this part of the investigation, the examiner will need to identify those brokers who deal with the bank. If a listing is not provided by the bank, the examiner should refer to telephone or broker association directories for the names of several brokers in the general vicinity of the bank's main office and/or its branches. (Note: The National Association of Real Estate Brokers is a predominantly Black organization.) Select a sample of brokers to be interviewed.

Obtain the following information from the owners of the firms or the registered brokers selected to be interviewed, who may be informed of the purpose of the interview:

- Name, address, sex, race and company name.
- Whether the broker has ever referred prospective loan applicants to the bank. If so, approximately how many per month? If not, determine the reason and what institution the broker does use and why.
- The names and addresses of other real estate companies that may send or have sent prospective applicants to the bank (specifically non-white brokers).
- The broker's understanding of the bank's loan policies with respect to minorities, including women, and integrated areas.
- The basis for the broker's understanding of the bank's policies. Included would be any aspects of the bank's reputation or any incident or experience that the broker may have had with the bank, even if the incident took place some time ago.
- Whether any employee of the bank or other person associated with the bank has ever instructed the broker (or any other broker or agent) not to refer certain types of applicants or applicants from a particular area. If so, obtain all details.
- The name, race, sex and last known address and place of employment of every person known to the broker to have been rejected as a loan applicant by the bank in the past two years, and the reason, if known. This information should also be obtained for each person discouraged by the bank from applying for or pursuing an application for a mortgage.

Contact with Consumer Groups

From time to time various civic groups conduct campaigns designed to combat "redlining" or other forms of discrimination. These groups are often aware of persons who applied for loans at various institutions. In some cases, a study may have been done or a complaint filed with a local, state or federal agency. If such groups exist in the area where the bank is located they should be contacted as valuable source information.

Obtain the following from the director or chairperson of each group:

- Name, address, race, and sex of the person interviewed, and the name and phone number of the consumer group.
- Information the groups may have concerning the bank's lending policy, including:
  - —Where loans will not be made and why;
  - —Where only FHA or VA loans will be made;
  - —Whether FHA or VA loans will not be made in certain areas;
  - —Where loans will be made at higher rates, shorter duration, etc., and
  - —Areas considered by the bank as high risk areas.

Determine the basis of the group's information.

- Information concerning other state nonmember banks believed to be engaging in racial redlining.
- Name, last known address, race and sex of any person known to the group to have been rejected for a loan by the bank within the past two years. If not immediately available, determine whether the organization can provide the names of such individuals to the Regional Office. Copies of any studies, analyses, position papers or other documents produced by the group pertaining to allegations of discrimination in lending.
- Name and address of any other person or group that the organization believes may have additional information in this regard.

RESOLUTION OF COMPLAINT

Refer to Investigative Report instructions in the General Complaint Investigation Procedures. The examiner will prepare the investigation memorandum and forward it to the Regional Office for review and preparation of the final resolution letters to the complainant and to the bank. The Regional Office will submit these letters without signature (in the case of Fair Housing complaints only) to the OCA for review before sending the resolution letter to the bank and the complainant. Whether or not the findings indicate any discriminatory treatment, the advisement of legal rights stated in the acknowledging correspondence should be restated. The OCA will return these letters of resolution to the Regional Office for mailing.

SUBSTANTIAL NONCOMPLIANCE

Review the ECOA/FHA Enforcement Policy Statement for guidance. Reviewing and testing general-compliance with fair lending statutes are part of the regular compliance examination and are expected to be performed at that time. The field investigation of a fair lending complaint should focus on the complaint that has been filed. This is not to say, however, that should the investigating examiner suspect or uncover evidence of substantial noncompliance that no action be taken. If this situation occurs, the Regional Office should be contacted immediately for instructions as to whether additional facts should be gathered or examiner(s) assigned to commence a special compliance examination.

SAMPLE DOCUMENTS

Several sample documents are provided at the end of this section. These sample documents are provided for guidance in preparing a response to a complainant alleging housing discrimination. These documents are a "Suggested Form Letter to Complainant," a "Suggested Form Letter to Bank," and a sample "Fair Housing Investigation Report."

Senator DIXON. I thank you, Mr. Bovenzi, and we are delighted to have Ms. Fitts here, the Assistant Secretary for Housing of the Department of Housing and Urban Development.

Ms. Fitts.

C. AUSTIN FITTS, ASSISTANT SECRETARY FOR HOUSING, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT, COMMISSIONER, FEDERAL HOUSING ADMINISTRATION [FHA], WASHINGTON, DC

Ms. FITTS. Mr. Chairman, thank you.

Chairman Dixon and Senator Riegle and members of the subcommittee, the Department of Housing and Urban Development appreciates your invitation to testify on the findings of our report on mortgage loan discrimination mandated by FIRREA.

In one of his earliest appearances before Congress, Secretary Kemp made the statement that the creation of new housing opportunity means little if housing opportunity is not equal for all.

The President and the Secretary are committed to the national goal of ending discrimination in the sale and rental of housing. Assuring there is no discrimination in mortgage lending for FHA insured loans is critical if that goal is to be met.

But, also critical is the need to find ways to ensure that we take steps in using FHA and similar programs to reach those neighborhoods most in need of mortgage credit for home ownership opportunities.

In order to meet our objective, we intend to coordinate and take full advantage of the resources of HUD's program offices, including the Office of Housing, which I direct, but also the Office of Fair Housing and Equal Opportunity and the Office of Policy Development and Research.

And if I might, I'd like to introduce to the members of the committee two of the people who will be working with me towards this important goal.

The first is the President's nominee for the Assistant Secretary for the Office of Fair Housing and Equal Opportunity, Gordon Mansfield.

And my Deputy Assistant Secretary for Single-Family who runs the entire Single-Family Program, Ron Rosenfeld.

Since 1980, HUD has had the responsibility under the Home Mortgage Disclosure Act to disclose publicly information on FHA Title I and Title II activity by mortgagee for metropolitan statistical areas and census tracts.

We have found that prior to 1988, HUD had not met its responsibilities under the 1980 act.

Secretary Kemp intends to carry out fully his responsibilities under HMDA, FIRREA and other statutes designed to prevent lending discrimination.

The 1987 Housing and Community Development Act expanded HMDA to include mortgage banking subsidiaries of bank and thrift holding companies and savings and loan service corporations.

Subsequently, the Department began geocoding census track information into the FHA data files for calendar years 1980 through 1988 for all metropolitan statistical areas.

Further statutory change has expanded on the types of data we must be provided by lenders. We have taken, and are taking, a number of steps to ensure non-discriminatory lending practices.

Let me mention to you five:

First, we are working with the Federal Financial Institution's Examination Council to measure, detect and eliminate redlining and other discriminatory practices.

Second, we are enhancing FHA's insurance operation systems to provide additional information. Currently, our system includes zip codes along with county and State locations of insured properties. We're in the process of enhancing the Home Underwriting Management System and the Single-Family Statistical System to include data on race, sex and income of the borrower and coborrower for improved transactions.

Other information under review for incorporation into this system includes data on the sale of mortgages and information on rejected borrowers.

Third, we are developing and monitoring reporting procedures for all nonsupervised lenders by utilizing our approved mortgagee file as a base to check the reporting compliance of lenders. We will be working with the Mortgage Bankers Association to cover any mortgage lenders who may not participate in FHA programs but are active in other areas.

Fourth, we are developing and monitoring various forms of credit discrimination and steering.

HUD's Office of Policy Development and Research will soon begin a project aimed at developing measures of the extent of geographic racial or other forms of FHA credit steering, as well as measures of FHA credit discrimination.

This will be the first time that HUD has attempted to establish definitions and standards in the area for use by our Office of Fair Housing and Equal Opportunity and the Federal Housing Commissioner.

Fifth, finally, all parts of HUD, including the Offices of Housing and Fair Housing, will work closely with other Federal financial regulatory institutions as well as other experts and the interest groups in this area in developing practical monitoring in enforcement approaches.

Secretary Kemp believes strongly that we need to go beyond the letter of our statutory reporting and data collection requirements and ensure that the information we receive is put to effective use in our enforcement efforts.

Ultimately, more needs to be done than merely accepting and processing mortgage insurance applications in a non-discriminatory fashion. We must battle any misperceptions that are inhibiting the flow of credit to qualified borrowers in all areas of our nation.

While the Government has no intention of forcing lenders to make bad loans or establish rigid lending quotas, we can and must do a better job of encouraging lenders to maintain prudent lending programs in all areas of their community.

A good credit risk shouldn't be denied the chance to buy a home merely because of the color of his or her skin or the location of his or her neighborhood.

I'd like to mention the Secretary has spoken in the Senate in many of his speeches about his concept of greenlining. We believe very strongly that, in addition to the normal distribution channels that FHA has used, with expanded outreach to financial institutions with CRA obligations, as well as to State and Local agencies working with nonprofits, there are real opportunities to describe what the Secretary has defined as greenlining.

I know Senator Cranston just asked what kind of legislative proposals we would recommend. The Secretary has indicated that he will be coming forward with legislative proposals on this very issue which we believe is critical.

Another step that the Secretary intends to use is increase powers under the Fair Housing Amendments Act of 1988, which went into effect on March 12, 1989.

In addition to adding to the protected classes covered under the anti-discrimination provisions of the 1968 Civil Rights Act, the act also dramatically strengthened enforcement powers for the Secretary of HUD in dealing with housing discrimination.

Mr. Chairman, Senator Riegle and members of the Committee, Secretary Kemp has made the commitment to use the full resources of the Department to stop the redlining of distressed inner-cities and rural areas and greenline those areas for success.

We look forward to working with your Subcommittee to meet the goals of equal housing opportunity and home ownership for all Americans in every part of this country.

Thank you very much.

[The complete prepared statement of C. Austin Fitts follows:]

STATEMENT OF C. AUSTIN FITTS
ASSISTANT SECRETARY FOR HOUSING--FEDERAL HOUSING COMMISSIONER
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
BEFORE THE
SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS
SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
OCTOBER 24, 1989

Chairman Dixon and members of the Subcommittee. The Department of Housing and Urban Development appreciates your invitation to testify on the findings of its report on mortgage loan discrimination, mandated by Section 1220 of the Financial Institutions Reform, Recovery and Enforcement Act of 1989.

In one of his earliest appearances before a committee of Congress, Secretary Kemp made the statement that the creation of new housing opportunities means little if housing opportunity is not equal for all -- if any individual or family faces discrimination because of race, age, religious belief, ethnic origin, handicap or family status.

We at HUD are committed to the national goal of ending discrimination in the sale and rental of housing. Assuring there is no discrimination in mortgage lending for FHA-insured loans is critical if that goal is to be met.

In order to meet our objectives and responsibilities, we intend to coordinate and take full advantage of the resources of all of HUD's program offices, including the Office of Housing and the Office of Fair Housing and Equal Opportunity and the Office of Policy Development and Research.

FHA has helped 17 million families realize the American dream of homeownership. During 1986 and 1987, for example, FHA insured roughly 2.3 million home mortgages. In 1987, more than a third of the homes were located in urban areas with the remainder in suburban locations and a small proportion in rural areas. Almost two thirds of the homes purchased with FHA went to borrowers with incomes under $40,000. The bulk of FHA transactions involved married couples but a significant share of the homes were bought by single heads of household. For example, slightly more than 20 percent of the mortgages were insured for single heads of household -- almost evenly divided between single males and single females. In addition, another 7.6 percent of the sales covered other related or unrelated individuals. Most of these consisted of parent-daughter, brother-sister or similar family combinations.

Since 1980, HUD has had a responsibility under the Home Mortgage Disclosure Act (HMDA) to disclose publicly information on FHA Title I and II activity by mortgagee for Metropolitan Statistical Areas and Census Tract. We have found that prior to 1988, HUD had not met its responsibilities under the 1980 Act. Secretary Kemp intends to carry out fully his responsibilities under HMDA, FIRREA and other statutes designed to prevent lending discrimination.

In 1987 Housing and Community Development Act expanded HMDA to include mortgage banking subsidiaries of bank and thrift holding companies and savings and loan service corporations. Subsequently, the Department began geo-coding census tract information into the FHA data files for calendar years 1980 through 1988 for all Metropolitan Statistical Areas. Further statutory changes have expanded on the types of data which must be provided by lenders.

We have taken, or intend to take in the future, a number of steps to assure non-discriminatory lending practices. These include:

-- Working with the Federal Financial Institutions Examination Council (FFIEC) to measure, detect and eliminate redlining and other discriminatory practices. A proposed rule, published October 6, 1989, includes the type of information lenders are now required to report (example: race, sex and income) and the types of reports that are needed from this data collected.

-- Enhancing FHA insurance operations systems to provide additional information. Currently our system includes zip codes along with county and state locations of insured properties. We are in the process of enhancing the Home Underwriting Management System and the Single Family Statistical System to include data on race, sex and income of the borrower and co-borrower for approved transactions. Other information under review for incorporation into the system includes data on the sale of the mortgage and information on rejected borrowers. currently data on rejected borrowers can only be found in the FHA case binder processed in our Field Offices. For cases processed under our Direct Endorsement program, we have no rejection statistics.

-- Developing and monitoring reporting procedures for all non-supervised lenders by utilizing our approved mortgagee file as a base to check the reporting compliance of lenders. We will be working with the Mortgage Bankers Association to cover any mortgage lenders who may not participate in FHA programs but are active in other areas.

-- Developing and monitoring various forms of credit discrimination and steering. HUD's Office of Policy, Development and Research will soon begin a project aimed at developing measures of the extent of geographic, racial or other forms of FHA credit steering as well as measures of FHA credit discrimination. This will be the first time that HUD has attempted to establish definitions and standards in the area for use by our Office of Fair Housing and Equal Opportunity and the FHA Commissioner.

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-- All parts of HUD, including the Offices of Housing and Fair Housing, will work closely with other Federal financial regulatory institutions as well as other experts and interest groups in this area in developing practical monitoring and enforcement approaches and procedures.

Secretary Kemp believes we need to go beyond the letter of our statutory reporting and data collection requirements and ensure that the information we receive is put to effective use in our enforcement efforts.

Ultimately, more needs to be done than merely accepting and processing mortgage insurance applications in a non-discriminatory fashion. We must battle the any misperceptions that are inhibiting the flow of credit to qualified borrowers in all areas of our nation. Many lenders still perceive that lending in the inner-city is inherently too risky. Others perceive that FHA programs must be changed if we are to make significant progress.

While the government has no intention of forcing lenders to make bad loans or establish rigid lending quotas, we can and must do a better job of encouraging lenders to maintain prudent lending program in all areas of their community. A good credit risk shouldn't be denied the change to buy a home merely because of the color of his or her skin or the location of his or her neighborhood.

As a first step toward improving the current situation, FHA intends to expand its outreach efforts toward financial institutions that traditionally have been reluctant to use our programs (i.e., insured depository institutions) and to encourage joint participation by lenders, community groups and non-profits in programs that would make FHA-insured loans in markets not now being served. Ideally, these programs would target income groups that are somewhat below the typical homebuyer and very modest-priced homes. In order to increase the likelihood of success, we envision a combination of front-end applicant pre-screening, ongoing counselling on debt management and home management, the commitment of community resources for housing and neighborhood preservation and, of course, flexible loan underwriting on the part of the participating lenders.

The Fair Housing Amendments Act of 1988 went into effect on March 12, 1989. In addition to adding to the protected classes covered under the anti-discrimination provisions of the 1968 Civil Rights Act, the Act also provided dramatically strengthened encorcement powers for the Secretary of HUD in dealing with housing discrimination.

The most effective way to detect lending discrimination is to gather the necessary data, and to examine the data so as to detect patterns which may reflect discrimination. Under authority of the Fair Housing Amendments, the Secretary of HUD can then file a complaint against the lender where that appears warranted.

Mr. Chairman, Secretary Kemp has made the commitment to use the full resources of the Department of Housing and Urban Development to stop the "redlining" of distressed inner cities and rural areas, and "greenline" those areas for success. We look forward to working with your Subcommittee to meet the goals of equal housing opportunity for all Americans in every part of this country.

Senator DIXON. Thank you very much, Ms. Fitts.

Let me say we're going to have a round of questions now by the panel, but if I may, I'd like to make this initial observation.

I think it to be somewhat incredible that the substance of the testimony is mostly that you haven't found any violations when the evidence is pretty clear out there that a lot of violations have to be taking place.

The standard statistics being that denials of black applicants are at least two to one. Mr. Fiechter has suggested what we already know, that in some of the great urban areas of this country, represented by some of the Senators on this panel, it goes much higher than 2/1—3/1, 4/1.

But, we have incredible testimony here. I mean no offense to anybody. Mr. Herrmann's suggesting that they had no violations that they could find, others finding I think five violations, suggested by Mr. Bovenzi; Mr. LaWare saying that they really found it to be remarkable there were so few.

I'm not trying to pick on anybody, but I want to suggest that I find it pretty close to remarkable that we never find any violations.

I do want to say that, Mr. Fiechter, at least in your case, I got the sense that you were doing something pretty substantive in the new program you started in January of this year, although I find it incredible that it takes until the end of next year to have it in place.

As a person who was an administrator, as a State Treasurer and Secretary of State, I found I could move faster than that in most cases when I saw problems.

Now, you know, there are a number of things suggested to us. Now, some of you touched on it. But we are using testers now in the marketplace with respect to sales and with respect to rentals, but I sense that we are not at all using testers anywhere in any of the agencies.

I hesitate to suggest that we would mandate that by law. We might have to. But, I see testers as a possibility here with respect to the question of discriminatory loans.

Some places are using on a voluntary basis mortgage review boards. It seems to me that all of your agencies could be working with the financial institutions under your jurisdiction to do some of that.

And consumer compliance examiners, you know, it's great to be concerned about safety and soundness. I give you all A's for that.

Everything I've heard, Mr. Chairman, has always been that we work pretty hard at safety and soundness. But I'm somewhat frustrated as the Chairman of the Consumer and Regulatory Affairs Subcommittee that nothing else seems to have that preeminence in any of the regulatory agencies. And we really have some information. I say to you candidly that you're so consumed with safety and soundness, which you should be concerned about, that consumer compliance questions are not much a matter of concern by examiners.

Now, Mr. Fiechter, I think you're trying to address that in what you're doing.

So I would just like to ask each of you whether you could come back to us separately from your agencies with some suggestions about what you can do to find new ways to address this problem in a degree of specificity that I at least see, Mr. Fiechter, in what you're trying to do there.

In other words, let me say this. If you have a black family with a man and a woman working, they're making, say, $35,000 a year, which most everybody—young people now both work. We all know that. Thirty-five thousand is certainly a number we could address here as a reasonable number.

If you can find that a black couple making $35,000 a year got turned down for a loan in a bank in Chicago, in my home State, but a white couple making $35,000 a year got that loan. And there's some degree of specificity.

Then I think we can find what's occurring here in some regard. I don't see any of that going on now. I want to be candid. I don't see that going on now.

We have this great system out there with all kinds of people involved and these great regulatory agencies. Nothing coming back to us.

Yet, the statistics are there, ladies and gentlemen. It's occurring.

I wonder, Ms. Fitts, what you would say about that.

Ms. FITTS. The use of testers is a very good point. As you know, we have had success using testers, particularly in the racial market.

Senator DIXON. Yes.

Ms. FITTS. Of the number of complaints we have received since the passage of the 1988 act, which, again, went into law on March 12 of this year, we have received approximately 6,000 complaints under that law.

My understanding is, of that 6,000, only six relate to lending practices. The others relate primarily to rental practices.

Senator DIXON. Well, of course, but the law now is only looking at sales and rental practices.

Ms. FITTS. Absolutely.

Senator DIXON. The law does not direct you now to look at lending practices.

Ms. FITTS. Absolutely. But I think there has been a preference to use testers in the areas where we are receiving the most complaints.

It is more complicated to use testers in the lending process, and you should understand that as we go forward and try to do testing.

One, to do good testing, you need to make a downpayment on a home. And, consequently, it's a more expensive process, if you will, to do a tester on a mortgage lending application.

The other is it's more difficult to run a control group on a tester, so that there are more complicated issues. But we agree with you that that is one good way to test discrimination.

Senator DIXON. OK.

Ms. FITTS. I do want to say one thing which I think is very important because, clearly, one of the tools that we must use at the Department is very strict enforcement against discrimination when we find it, particularly in the FHA program.

But there is something also very important and that is to recognize that there are very serious economic barriers to getting those neighborhoods served in volume.

And that is why I think it is so important that when the Secretary comes forward with his greenlining initiatives, that it receive your full attention, because we need not only use the stick, but we also need to use the carrot very aggressively.

Senator DIXON. Well, see, nobody comes here to quarrel with you about the fact of the obvious things that we know out there. You know, the poor have less ability to obtain loans. We accept that. And there are more poor among the minority groups and we all understand that. What we are concerned about is the obvious, that, unfortunately, notwithstanding all that, we have plenty of folks among our minority groups in difficult neighborhoods in our inner-cities in America and other areas as well who, though qualified, are obviously not receiving these loans.

Now, what are we doing about it as a great nation?

I think it's a terrible challenge for all of us. Nothing is more important than the ownership of a home.

And I can't think of anything more frustrating than a married couple out there that happen to be a minority couple that are making a decent income and can't get a decent loan at a financial institution. We have got to do something about it.

Mr. Herrmann, here is this great organization of yours. You know, the Comptroller does good work. You can't find any violations out there. It's remarkable.

Mr. HERRMANN. Yes.

Senator DIXON. I don't mean to be offensive about it.

Mr. HERRMANN. No, no, Mr. Chairman. Now, Mr. Chairman, I thank you for the compliment with respect to the safety and soundness, but——

Senator DIXON. Well, I mean it sincerely.

Mr. HERRMANN. But, what we've been searching for, Chairman Dixon, is the equilibrium here of how much attention, resources do we put to compliance, and how much to safety and soundness?

For the last 2½ years, Mr. Fiechter mentioned what the thrift folks are doing now, we have embarked on the same attempt. We have separated out our compliance effort. And we are——

Senator DIXON. You have now separated out compliance on——

Mr. HERRMANN. From safety and soundness.

Senator DIXON. From safety and soundness.

Mr. HERRMANN. Yes, sir.

Senator DIXON. Incidentally, I would suggest to you that's not a bad idea. The overwhelming evidence we have coming back to us, Mr. Herrmann, and I don't mean this offensively, I can see how a guy out there or a lady or a gentleman that's an examiner might think, gee, this safety and soundness thing, this is a big deal. If the bank fails, I'm in trouble. But, you know, nobody's going to get real mad about these other, you know, questions that are before me.

And so I think that's a good idea, may I say, that you are looking at these consumer questions as a separate question from safety and soundness. Now, to what extent are you doing that now?

Mr. HERRMANN. Yes, we have embarked——

Senator DIXON. And how recently did you do it?

Mr. Bovenzi is still studying, I think.

Mr. HERRMANN. Yes. We began our process in April of 1987, Mr. Chairman, and we have been very, very pleased with the success.

Senator **Dixon**. Well, you haven't found any violations. I'm not too pleased with that. There must be some out there——

Mr. **Herrmann**. I understand.

Senator **Dixon**. I don't mean that offensively.

Mr. **Herrmann**. I understand your position on that.

But what we have really accomplished here is by a random sampling of banks, we have come forward with a concerted effort on those banks, a very, very thorough examination, which really entails scrutiny of the records.

And I think the result really has been excellent. And we do have some performance statistics to really evidence that.

Senator **Dixon**. The Senator from Michigan, the distinguished chairman of the Banking Committee.

Senator **Kerry**. Mr. Chairman, before the Senator from——

Senator **Dixon**. Yes, of course. Senator Kerry.

Senator **Kerry**. I would beg your leave for a moment, if I may. I have to go have a meeting preparing for the Mutual Legal Assistance Treaties that I'm managing.

I just wanted to ask if the record could remain open so that I might submit some questions.

Senator **Dixon**. Of course.

Senator **Kerry**. And I do before leaving want to associate myself with the concerns that you expressed and that line of questioning.

I think this is a very important hearing and I congratulate you on holding it, and express just before I leave, my deep concerns about the disparity between the evidence as reported in so many studies, as well as the articles of the Atlanta Constitution and others, and our own Boston situation, and the disparity between that evidence and the seeming evidence that your efforts as of this moment displayed.

And I would certainly want to pursue that in a line of questioning.

But I thank the chairman for leaving the record open.

Senator **Dixon**. Well, I thank the distinguished Senator from Massachusetts.

We're delighted to have the Senior Senator from Florida, Senator Graham, here as well.

And in due course, we'll recognize each person for a statement. I'm anxious to have the questions of the distinguished chairman of our Banking Committee, who we're honored to have here at this hearing.

Senator **Riegle**. Well, thank you, Mr. Chairman, and I'm ready to pose some questions. I'm just wondering, if I may, if the Ranking Minority member wants to go next, and then I'd be happy to follow him if he wishes?

Senator **Dixon**. I'm delighted to recognize him. He had quietly indicated to me he was not in a big hurry. But I'm delighted to recognize the ranking member first if he cares to.

Senator **Bond**. Thank you, Mr. Chairman. I appreciate the courtesy, but I'll save my opening comments and questions until our chairman is finished.

So, go ahead.

Senator **Dixon**. Very good.

Senator **Riegle**. Thank you, Senator Bond.

I think what we've heard this morning is very important testimony and I'm very anxious as well to hear what we will learn from our second panel.

I have to say, however, that I share a lot of the concern and frustration, I think, proper frustration, of Chairman Dixon in the fact that we still seem to be going quite slowly here. And more slowly than is justifiable or than the need requires.

I don't think safety and soundness properly should be mixed into this issue of discrimination. I think, when that's used, it's often used as a smokescreen and as a cover. There can be no basis for discrimination, whether it be on race or geography or other factors, where you otherwise have a proper mortgage applicant and package that's come forward.

And if there's one thing this country has to do, it is to see to it that there's equity in terms of how these opportunities are available to our people.

So, the notion of splitting apart the effort of really looking at discriminatory patterns or practices should be separate and apart from some sort of cosmic argument about safety and soundness.

There are sound credits by individual mortgage seekers in all circumstances, and they ought to be on an equal footing. And they ought to be so adjudged when they come forward for mortgage credit.

Now I have to say in line as a follow-up to what the Chairman has said, Mr. Herrmann, that when I look at the OCC's report on Mortgage Discrimination pursuant to Section 1220 of FIRREA, that it's barely over one page long.

Now you indicate that you folks got rolling on this in April 1987, so it's not as if this is an issue that you've just recently turned to. But, as I read your report here, it states that the OCC does perform, quote, "a limited number of analyses on individual national bank mortgage acceptance and rejection data," but declines to analyze any of the data because they are, quote, "not readily retrievable." And, quote, "have limitations."

Now, when I read section 1220, I don't see any escape clauses for cases where data are not readily retrievable or have limitations. Seems to me you've got an affirmative obligation to get out there and get this work done, and without excuses, because as I've heard others on this committee say over a period of time:

Justice delayed is often justice denied.

And so we've got folks out there who are being turned away in the mortgage market improperly and unfairly. That is a matter that needs remedy now, not 6 months from now or 6 years from now or 26 years from now.

So, seems to me, you've got an affirmative obligation to dig into this more deeply. We have some proper expectation to have from you an analysis that is in much greater detail than what you've given us.

Mr. **Herrmann**. May I respond, Senator Riegle?

Senator **Riegle**. Please.

Mr. **Herrmann**. I'm sorry. There must be really a miscommunication on that particular point because we are, in fact, analyzing institutions on a bank by bank basis where we have any belief at all that there is a problem there with respect to discriminatory lending.

I believe the intent in our report was to relay to the Congress the fact that, on a general basis, for all institutions, that information was not retrievable.

So what we have done really is targeted institutions based on a belief, a complaint.

Senator **RIEGLE**. Well, what do you have for us?

Mr. **HERRMANN**. I think there, Senator, what I might do is suggest that we've had some conversations with staff about the report itself. And what I would like to do is amend that report to really add information along this line.

I also think, and I want to explain this, FIRREA really called for rejection/acceptance rates across the system, at least that's how we interpreted it, along with recommendations.

And though our report, I must admit, is brief, we felt it was important to be straightforward and explain the difficulty of where we were right now.

With respect to the recommendations, a good bit of work has gone on through the summer at a task force level.

And our judgment was that we did not want to preempt that decision process.

Now, I think there's a good bit of work going on and our judgment is that we will probe those particular alternatives and others that might come forth. And I simply want to reiterate to you our commitment, similar to yours.

If there is a problem here, we sure want to get at it as well.

Senator **RIEGLE**. Well, I think at a minimum, you need to sit down and go through what details you have. I mean, you in effect say you have other information that you've not put in your summary, and I think that has to be shared with the subcommittee.

Let me just raise one other thing at this point with you, Mr. LaWare.

The Federal Reserve Board's report on mortgage discrimination under Section 1220 seems to me to be also essentially a nonreport. In effect, the Fed just says: Quote "We lack any relevant data," and proceeds to discuss various reports in the existing literature on mortgage discrimination.

And I recognize that the Fed may not have any significant data on mortgage rejections as such, but it does have or certainly should have an enormous data base on mortgage originations complied pursuant to the Home Mortgage Disclosure Act.

And I'm wondering why the Fed couldn't have used that data in combination with demographic information that's available from the Census Bureau to at least reach some kind of tentative and informed judgments and conclusions about mortgage discrimination with whatever caveats one wants to file with it.

But it seems to me you're in a position to dig in here more than it seems to me that you have. And I think you ought to.

Mr. **LAWARE**. Well, under the changes in HMDA that were put in as part of FIRREA, we will now have much more complete information dealing with applications by sex and by race, and so forth, so that as that information starts to come through and as we aggregate it, we'll be in a much better position to answer that kind of a question.

We simply don't have the data in the form that's necessary to make the kind of response that you're looking for, Senator.

Senator **Riegle**. Well, I've made my point. I've heard your response. My time is up.

Let me just make one other point, Mr. Chairman, before yielding to Senator Bond and back to you.

And that is that we have now had eight Senators here this morning present and participating in this hearing. And I think that alone is a measure of the importance that the committee attaches to this work of the subcommittee. There is a message in that, and I'm sure it's not lost on the regulators present.

Senator **Dixon**. I think that's a very good and important observation. I thank the Chair for that. We're delighted, of course, to have the ranking member here for this important hearing, the distinguished Senator from Missouri.

We're glad to have the Senator from New York join us. And we'll be with him shortly.

Senator Bond.

OPENING STATEMENT OF SENATOR BOND

Senator **Bond**. Thank you very much, Senator Dixon. I do, too, join in commending you for holding this hearing because I think it's absolutely essential from what we've learned not only in this hearing but previously. And certainly from all of that evidence as well as this testimony, I don't think there's any doubt that while we may disagree about the extent of discrimination, it certainly does exist. There is a problem. And we are committed to doing something about it.

Access to credit is essential in helping Americans realize their dreams of a better life for themselves and their children.

If entire neighborhoods are receiving fewer loans simply because of the color of the skin of the people who live there, we should be alarmed. We are alarmed. We need to be looking at ways to remedy this.

Now, maybe the examination practices that have gone on so far have not disclosed significant blatant discriminatory violations. It may be a much more subtle, more complex practice that's going on here.

If so, then we've got to find ways of dealing with that, ways outlined previously by Secretary Kemp: green lining, enterprise zones, affirmative ways of dealing with discrimination may be the way that we have to go.

But I'm also interested in the differing attitudes of some of the organizations. And while we've touched on it before, I noted in the written testimony from the Federal Reserve, there was a statement:

> The Board believes that expecting a bank examiner to master both safety and soundness and consumer affairs, civil rights aspects of bank examinations is not practical given the existing complexities of both areas, which continue to increase.

Now, I'd like to know from Mr. Herrmann and Mr. Bovenzi if there will be separate compliance departments or is it going to be separate—are you just having people who have special training in consumer affairs, civil rights?

Mr. Bovenzi?

Mr. **Bovenzi**. Well, Senator Bond, I'll address that in two parts. What we've proposed in our testimony is to have separate community affairs specialists who would be part of our Office of Consumer Affairs rather than part of our Division of Supervision.

These people would be required to meet with others in the community to find out what the concerns were and then pass that information on to the examiners.

So that is one part. As you are aware, with our examination staff, we have not had separately trained compliance examiners and separately trained safety and soundness examiners.

Our reason for that in the past, as you know, has been to give us greater flexibility to meet increased workloads as they appear. We agree that both compliance and safety and soundness are important concerns. If they are two separate issues, we need to address them both to the extent we can.

We are now seriously considering having specially trained compliance examiners for whom that would be their career path. They would be part of our Division of Supervision.

We have not yet acted on that but are seriously considering it at this point.

Senator **Bond**. Would you disagree with or are you ready to accept the contention made by the Fed that they have to be separately trained?

Mr. **Bovenzi**. I would agree that both fields are becoming more and more specialized and complex, and it's just becoming more apparent that the generalist approach is harder to maintain.

Senator **Bond**. Does that mean we're going to see separate civil rights personnel?

Mr. **Bovenzi**. We are certainly going to see it in our Office of Consumer Affairs. I am not trying to say no——

Senator **Bond**. I know you don't have the final responsibility but I believe this Committee would expect that the answer would be yes—just as a hint. [Laughter.]

Mr. Herrmann?

Senator **Dixon**. As a hint, I agree.

Mr. **Herrmann**. Senator Bond, there is no question about the need for special training and for specialism in many of these areas. But we have found—we went through this effort in the late seventies, where we totally isolated our Consumer Training and our Consumer Examinations.

Our current approach is to take the benefit from that experience. And we have altered our way and we think we're in the best mode right now. And that is separate examinations but using examiners who've had both safety and soundness understanding and experience and specialized training.

I'd like to add, and I happen to have the number, since January 1986, we have trained 1,088 examiners for a 4-week period, throughout the course of this period, since January 1986, on these specialized areas. That is, fair lending, CRA and so forth.

I want to add one other point, Senator Bond, since I have this opportunity.

The trick with respect to supervision in these specialized areas is to be able to communicate with bank management and bank boards of directors. And there is where we find the more generalist skill; the examiner who understands the whole bank is really invaluable.

Now it is, again, the balancing, the very difficult balancing at times. But, if we have an examiner who only knows that singular narrow area, we have found that they are not as successful in explaining to top management, the decision-makers, and to the boards the nature of the problem and how to go about solving it.

Senator **Bond**. So you just flat disagree with the position of the Federal Reserve?

Mr. **Herrmann**. No, sir, I think the distinction here is we believe in specialism and not specialists. Now, maybe the distinction is a tough one, but in some areas, you can use the knowledge across a broader plane. But, for fair lending we have decided to train in locales a special person who has that ability to go in and dig this up.

Senator **Bond**. Governor LaWare, would you like to comment on that?

Mr. **LaWare**. Our experience with the separation of those activities goes back more than 10 years. We have in each of the 12 Federal Reserve District Banks, a community affairs officer whose work is generally to work with community groups and to find out what their concerns are.

And then, using that information, to key the special examiners on compliance to look for a particular problem.

I might add that our experience with complaints charging discrimination may be helpful to the committee. We get somewhere between 2,000–3,000 complaints a year directed to the Federal Reserve Board for various reasons. Less than 150 of those complaints last year had to do with discrimination.

And I think that the mechanism exists there. The fact that the complaints are not being filed indicates to us that either consumers are not aware of the opportunity to lodge a complaint, or they are intimidated by the process, or the problem doesn't exist to the extent that the raw figures with regard to mortgages would seem to indicate.

Senator **Bond**. Would you therefore say that more consumer education and information would be an essential component of any program?

Mr. **LaWare**. Yes, sir, absolutely. Plus, more education for lenders as to what kinds of practices they need to eliminate from their procedures in order to comply.

Senator **Bond**. Thank you, Mr. Chairman.

Senator **Dixon**. I thank the ranking member.

The distinguished Senator from Florida, Senator Graham.

Senator **Graham**. Thank you very much, Mr. Chairman.

On September the 8th last year, this committee held an oversight hearing on the same subject and used as a starting point for some of our discussion newspaper accounts which had recently appeared in Detroit and Atlanta papers relative to discriminatory lending practices.

One of the persons who testified at that time was Mr. Manuel Johnson on behalf of the Federal Reserve. And he stated relative to the Detroit situation that:

> I don't feel like I can make a complete comment on that until we have completed our statistical study as to verification of the facts there and a verification of the results.

Mr. Johnson went on to state:

> We have not completed the Detroit assessment and we would be happy to communicate our findings when we do.

Mr. LaWare, could you give us a current status report as to where the Detroit investigation is?

Mr. **LaWare**. I can't respond to that specifically because I don't know what Vice-Chairman Johnson was referring to specifically.

Our research seems to confirm the raw statistical data in the Detroit report. That is, that the number of mortgages made in census tracts that are predominantly minority tend to be fewer in relationship to the housing units than in white census tracts with the same income characteristics.

The difficulty is that those statistics do not include the activities of mortgage companies. Mortgage companies historically have been much more active in making mortgages to minorities because they are heavily involved in VA and FHA supported mortgages. Banks are not notably aggressive in VA and FHA lending, simply because of their own internal practices.

So those statistics are missing and there may be some distortion, therefore, as a result of that.

So it's very hard to draw conclusions from the research that's been presented in Atlanta, in Detroit and again in Boston.

Senator **Graham**. My concern is that it's now been over 13 months since that statement by Mr. Johnson. And to my knowledge, we have not received the response that this called for.

I would like to urge that some sense of expedition be given to this assignment and that, as soon as possible, it be completed and forwarded to the committee.

Mr. **LaWare**. I believe a report was filed with the committee, but I don't know the date of it, sir.

Senator **Riegle**. If we could verify.

Mr. **LaWare**. If it hasn't been, then we will certainly file it.

[Information referred to follows:]

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

ALAN GREENSPAN
CHAIRMAN

October 19, 1988

The Honorable William Proxmire
Chairman
Committee on Banking, Housing, and
Urban Affairs
United States Senate
Washington, D.C. 20510-6075

Dear Mr. Chairman:

Thank you for your letter of July 26 asking us to review a four-part series of articles published in the Detroit Free Press that discussed a study conducted by the newspaper of lending patterns by the major financial institutions in Detroit. In particular, you expressed concern about the study's reported finding that the home purchase lending patterns of the largest institutions in Detroit reflect a difference in lending between predominantly white and predominantly minority middle-income neighborhoods that escalated each year from 1982 to 1986, reaching a ratio of about 3 to 1 in 1986 (white versus minority). You draw a comparison between this series of articles and a series of articles that appeared in the Atlanta Constitution in May, which I discussed in my letter to you dated August 8.

Indeed, there are similarities between the two studies, as well as significant differences. They both raise important and complex issues about the residential lending patterns of financial institutions in major U.S. cities. In both studies of home mortgage lending an attempt was made to control for factors other than race that might explain the differences in lending concentration. To do so, the Free Press study attempted to identify predominantly minority and white census tracts in the City of Detroit based on 1980 census data that are basically characterized as middle income. It then compared the rates of lending by these institutions for home mortgages per 1000 homes and found the differences mentioned.

As was the case in our review of the Constitution study, we do not question the general accuracy of the lending numbers presented in the Free Press study. We do, however, note that those who conducted the Free Press study may not have been able to obtain reliable statistical information on population changes since the 1980 census, unlike the Atlanta study where a source of apparently reliable information was available. Consequently, there may be some question about the accuracy of the characterization of the racial make-up of the census tracts studied. This is potentially important since the Free Press essentially assumes that loans in predominately minority areas are extended to nonwhites and loans in predominately white areas go to whites. However, if substantial neighborhood change has occurred in neighborhood racial composition since 1980, this assumption may not be valid. In particular, gentrification could result in loans in predominately minority areas going to white families. Similarly, integration of previously predominately white areas could mean that some loans that are assumed to be going to white families are in fact going to nonwhites.

Assuming the Free Press characterization of the data is correct, as I stated in my response to you about the Atlanta study, the numbers and anecdotal information presented with them are subject to many possible interpretations. One possible interpretation is that the numbers suggest a pattern of illegal discrimination based on race. However, as we pointed out in our review of the Atlanta study, many other factors may account for the differences in lending patterns, as well.

For example, differences in demand for loans in the census tracts in the study may account for the different levels of lending. In the Atlanta study an attempt was made to control for demand factors by reviewing lien transfer data to determine the actual number of transactions completed and to adjust the ratios accordingly. The Free Press study does not do this. The study did point out that the white neighborhoods in the study generate twice as many applications for mortgages as the minority neighborhoods. Though applications are not as good a proxy for demand as actual transfers, all else being equal, one would not find it intuitively surprising that a higher number of mortgage loans are generated from locations that generate higher numbers of applications for those loans. This intuition is supported by other data reported in the Free Press articles that focus on home lending by mortgage companies. Extrapolating from data on the market shares of all mortgages extended by mortgage companies in the neighborhoods in the study, it appears that the demand for home purchase loans in 1986 was approximately twice as large in the predominately white areas as it was in the predominately minority neighborhoods. Consequently, the lending figures reported by the Free Press appear to reflect, in substantial part, demand factors.

Some of the other factors that may have caused lending differences that were discussed in our response to the Atlanta study may be at work in Detroit, as well. In fact, the Free Press contains some anecdotal evidence supporting some of them. For example, the institutions' marketing efforts may not attract mortgage applicants from all segments of the community equally. It may be that the system of mortgage referrals by real estate agents doing business in the minority neighborhoods does not operate in such a way as to fully include the financial institutions. Customer preference for one type of loan over another (e.g., FHA versus conventional mortgages) or one type of lender over another (e.g., mortgage companies versus banks or savings institutions), or a combination of the two, may also help to explain the differences.

It is not my purpose by repeating those possible alternative causes to reject out of hand any notion that these lending differences may have been caused by discrimination. I do believe, however, that the statistics and other evidence contained in the articles do not, of themselves, necessarily lead to that conclusion. One aspect of the Detroit situation, that is mirrored in the Atlanta study, that leads us away from the conclusion that discrimination is at work is the fact that the lending institutions generally show a marked difference in their patterns of home improvement lending when compared to their patterns of home purchase lending. Many of the institutions in the study are significant home improvement lenders in the city, typically lending more heavily in predominately minority middle-income areas than in predominately white middle-income areas. For example, in 1986 banks and thrift institutions extended roughly four times as many home improvement loans in predominately minority middle-income areas as they did in predominately white middle-income neighborhoods. For the entire 1981-1986 period, the predominately minority areas received over three times as many home improvement loans as did the predominately white neighborhoods. It seems somewhat unlikely that an institution that is truly discriminating on the basis of race (or any other prohibited factors) would do so with respect to one type of loan but not another.

In fact, our examiners have not cited Comerica (the only bank in the Free Press study that we directly supervise) or any of the other much smaller banks in the surrounding suburbs that we supervise for improper discrimination. This is true despite years of what we believe have been in-depth and thorough examinations that look at all aspects of a bank's lending policies and practices, not just the statistics relating to one area of lending. If our examiners do find illegal discrimination, I assure you that all appropriate measures to correct the situation will be taken.

Determining the presence or absence of lending discrimination is, however, not the end of the inquiry when dealing with the Community Reinvestment Act. Our approach when conducting examinations or considering applications is to consider all of the types of lending a bank does in its community, and how well that lending meets community credit needs. Our analyses consider not only home lending (where that is a credit need), but also lending of other kinds that meet other needs. I was gratified to note that the Free Press articles contained information about the financial institutions' involvement in other types of credit, such as small business, redevelopment, and government program lending.

Where we have found CRA deficiencies, whether or not there has been any indication that improper discrimination was involved, we have tried to determine the root causes and have taken the steps necessary to get the institution to address the situation. We have done this in the Detroit area as well as in other parts of the country.

We have often found that deficiencies in community reinvestment lending by banks are caused by such things as the lack of a management program to institute and monitor lending efforts directed toward meeting the institutions' responsibilities under the CRA. This has often been reflected in the lack of organized efforts by the institutions to do community outreach to assess credit needs or to market and advertise their lending services. We have also found that deficiencies are caused by a lack of knowledge by bankers regarding the specialized techniques that can be employed to reduce the risk involved in a redevelopment project to acceptable levels through use of government assistance programs and other public/private partnership opportunities.

Our approach has been to work with the institutions to get appropriate policies and management structures in place to deal with their CRA responsibilities. We have also instituted a program within the Federal Reserve System for educating bankers in community reinvestment techniques and have sponsored numerous conferences and seminars on community reinvestment issues over the years. In fact, the Federal Reserve Bank of Chicago held such a conference at its Detroit Branch in June of this year at which the Board's Governor Martha Seger was a featured speaker.

We have taken this approach because we believe it properly reflects the Act's requirement that we encourage banks to help meet their communities' credit needs. When properly followed, such an approach will naturally lead to solid lending in the banks' communities without resort to allocating credit by the federal regulatory agencies, which the Act's legislative history indicates was not intended by the law in any event.

We can all debate whether progress in this area has been fast enough and substantive enough in Detroit and elsewhere. I was struck by the concessions by some of the Detroit bankers that they could do more in this regard and was encouraged by their assertion that they were willing to do more when they found the appropriate lending vehicles. I was also struck by some of the articles' assertions of the reasons Detroit bankers may have perceived too much riskiness in some of the developmental lending efforts that had gone unfinanced or that were financed by outside financial institutions--the cyclical economy of Detroit which is so tied to the fortunes of the automobile industry, a history of serious problems with development projects, such as the Renaissance Center, and a history of losses due to difficulties with the local field office of a federal agency. Perhaps, these concerns, if they exist, are erroneous or outdated. Our effort should be to encourage banks to organize, manage, and educate themselves about the lending needs and opportunities in their communities so they can assess, in a realistic and up-to-date fashion, the current risks and rewards for themselves.

I believe our approach to these matters in Detroit and elsewhere has been sound and consistent with the law's mandates. As I indicated earlier in this letter, this is an important and complex area. Both the Atlanta Constitution and the Detroit Free Press should be commended for participating in the dialogue about these issues. I remain convinced that there are few easy answers in this area and I do not believe the newspapers intended to imply that there are. But we must all take care when looking at studies such as these to look at the entire set of possible causes before reaching a conclusion.

Sincerely,

G.Loney:rlh
G-149,88-4315

bcc: Mr. Loney
Vice Chairman Johnson
Gov. Seger
Glenn Canner
Mrs. Mallardi (2)

[illegible]

United States Senate
COMMITTEE ON BANKING, HOUSING, AND
URBAN AFFAIRS
WASHINGTON, DC 20510-6075

July 26, 1988 #149

The Honorable Alan Greenspan
Federal Reserve System
Washington, D.C. 20551

Dear Mr. Greenspan,

The Detroit Free Press reported this week that it has developed considerable evidence that banks and savings institutions in the city "can do more" to meet Detroit's credit needs. The Free Press - U. of Minnesota investigation of lending practices in the metropolitan Detroit area documented racial patterns in mortgage lending, and found that the lending gap between white and black neighborhoods increased each year between 1982 and 1986, reaching a 3-1 ratio. A state official after reviewing the newspaper findings said "The conclusion is inescapable that significant disinvestment has occurred," and continued, "Once it's started, it's hard to turn around."

These are alarming allegations -- particularly the charge the racial discrimination in home lending persists. If verified, they signal a clear need for strengthening CRA enforcement throughout the U.S. I am writing to ask your agency to examine the Free Press report. I would like to know whether your agency has found similar patterns through conducting CRA examinations in the metropolitan Detroit area. If you have found such patterns, what steps have you taken to correct the deficiency? If you have not, how did the CRA performance of the commercial banks mentioned in the article differ from the performance of the banks as reported by the Free Press?

It appears to me that the Detroit Free Press study has revealed a pattern of lending similar to that recently found in Atlanta by the Atlanta Constitution. I wrote asking you to examine the Atlanta findings, and to take steps to ensure that the intent of the Community Reinvestment Act is being carried out. I am writing now, on behalf of the Banking Committee, to ask that you do the same in Detroit.

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I believe we are indebted to both newspapers for investigating a serious urban problem. The least we can do, you as the agency responsible for regulating the lending institutions, and we as legislators, is to respond to the findings that have been presented to us. I look forward to receiving your response.

Sincerely,

Bill Proxmire

William Proxmire
Chairman

WP:rem

Senator **Graham**. Whenever I read a newspaper account such as the——

Senator **Dixon**. I must apologize and say to the Senator from Florida my staff does not know about such a report being filed. We will look into that and advise the Senator from Florida at the earliest opportunity.

Senator **Graham**. Thank you, Mr. Chairman.

Mr. **LaWare**. The date was October 19, 1988, and it was addressed to Senator Proxmire as the then chairman of the committee, sir.

Senator **Dixon**. Well, I thank you, Mr. LaWare. We'll look that up and we'll distribute it among the members of this panel.

Mr. **LaWare**. Thank you, sir.

Senator **Graham**. Whenever I read a newspaper account such as the two-sided question, what comes to my mind is:

Where was the shortfall in the network, the safety screening of regulatory agencies or congressional oversight committees that resulted in this matter escaping our attention and having to be brought to us through an independent newspaper investigative report.

I'd be interested maybe starting with the Comptroller of the Currency as to what data is monitored as the indicators of general performance or nonperformance of a financial institution's responsibility under this act.

Mr. **Herrmann**. Yes, sir, Senator Graham, let me attempt.

There is a great problem here and that is our review begins at the application stage. And if we have any evidence that a bank is discriminating in any way, then there is a format that we use, and it's called the Home Loan Data System Analysis, in that we use the bank's records and we input format with respect to income, gender, the credit criteria, and we match that off with respect to rejections versus approvals.

And this is where the difficulty is, in my personal judgment. An institution that is having a problem here, where there is discrimination, it doesn't happen at the record stage. It's involved in the subtle stages previous to the application stage.

So, with respect to the chairman's question about where is the evidence, I think that is the difficulty here. What we see is the application record.

Senator **Graham**. But the newspapers had looked to certain statistical indicators that raised the question of whether there was a practice of invidious discrimination as opposed to the application of sound lending practices.

The statistical information won't necessarily answer the ultimate question, but at least it causes you to ask the ultimate question.

Are you satisfied that you have a screen of data collection that will put you in the position to know when to start to ask that question?

Mr. **Herrmann**. I think, Senator, some of the changes that have been recently made in FIRREA will be helpful. It will give banks a profile, an aggregated profile of where they are in the marketplace with respect to distribution.

But, with respect to the issue of discrimination on a single customer, I find in my judgment that that is an extremely elusive issue for us because we need evidence if we're going to charge a bank with discrimination. That's a very serious charge, and it should be.

Senator **Graham**. I agree with that, and it should be done with great discretion. But it is also one of the responsibilities of the bank charter to serve the community for which they are franchised. And it is your responsibility, as a regulator, to assure that all of the responsibilities of that charter are being discharged.

It seems to me that it is critical that there be a method of inserting the thermometer into the institution to determine whether there is a pattern of internal behavior that is inconsistent with their charter responsibilities. And that we in Congress have the responsibility of assuring that you have such a thermometer and are reading it on a regular basis.

Mr. **Herrmann**. I think your observation is correct, Senator Graham, and I think we do have the thermometer. And I think the new tools will really improve on that.

Senator **Graham**. Thank you, Mr. Chairman.

Senator **Riegle** [presiding.] Thank you, Senator Graham.

Senator D'Amato.

Senator **D'Amato**. Mr. Chairman, let me compliment the committee, and particularly Senator Dixon, for holding these important hearings. Discrimination in home mortgage lending strikes at the heart of one of the central promises that America holds.

And for generations, people have flocked to the shores of America, the dreams that a free economy offers, a job, a home and an opportunity to educate our children being one of those great inducements.

And I believe that the home represents the cornerstone of a sound financial future for nearly every American. And crucial to that realization of the sense of security and the sense of pride that home ownership provides is obviously the ability to obtain financing, a mortgage.

So let me ask this question, Mr. Herrmann.

The Atlanta Constitution reported this past January that the Office of Comptroller General, or Comptroller of the Currency examines only 35–50 banks a year for fair lending issues out of 4,500.

Is that true?

Mr. **Herrmann**. I believe, Senator D'Amato, that that information is not accurate unless the reporter is commenting on the more severe analysis of the Home Loan data analysis, not the Humda analysis.

Senator **D'Amato**. Would you care to make a distinction?

Mr. **Herrmann**. Yes, sir. The Humda data is simply a distribution analysis. The Home Loan data analysis is one that deals, the penetration, with respect to the credit criteria in each bank.

Senator **D'Amato**. Well——

Mr. **Herrmann**. Now, since April of this year, I'm aware that we have done 29 of those analyses and we did those in instances where we felt subjectively that we potentially had a problem in that institution with respect to possible illegal discrimination.

Senator **D'Amato**. Well, if, indeed, we're looking at a handful of banks as it relates to the practice of red-lining, that certainly sends the wrong message out.

If, as you have indicated, that there are many more banks that are being looked at but it is only in terms of those that would indicate a potential problem that the author of this article is writing about, and that's how you would explain why it's only 35–50 get the in depth review, that's where your initial inquiry leads you to.

Is that what you're——

Mr. **Herrmann**. Senator, I'm sorry. My staff has given me better information.

There were 700 banks in our sample in 1988 and in that sample, we did an affirmative effort to determine specifically, transactionally, if there was any evidence. And in only 29 did we find red flags.

So the sampling was much broader. OK?

Senator **Graham**. OK. That certainly is a much better indication. I think it would be a terrible stain to think that we're only looking at 35–50 banks in the course of a year.

Now I think the problem is much more pervasive. And I think Commissioner Fitts—and I had an opportunity to read her testimony and I want to commend the Secretary for her insightfulness. And I'm wondering who would care to comment. Maybe Mr. Herrmann, you would.

But, red-lining obviously is a problem of which we are aware. And that needs to be addressed. But, even if it were eliminated, we would still face the lack of green-lining, a lack of salesmanship, a lack of creating incentives for lending institutions to market mortgages in low-income neighborhoods or in urban centers.

Would you care to address that issue? Isn't that really the basic problem that we have in addition to those who deliberately break the law—and they are when they're red-lining, how do you undertake the problem as it relates to creating incentives? And greenlining?

I'm going to ask Commissioner Fitts if she doesn't see this as a problem.

Ms. **Fitts**. Certainly, redlining is a problem. I think that I wouldn't describe greenlining as a problem, since obviously we believe that it can be done.

Currently, the FHA distributes the majority of its mortgage credit through the private sector. That sector in many of these distressed areas, Senator, does not have the incentives to go into those neighborhoods.

We believe there are a number of interesting developments which have all occurred, that have come to a head at once, one is institutions more and more are taking their responsibilities under CRA very seriously.

Also, a network of state and local agencies in the housing area have grown up along with many nonprofits who were able and interested in providing the necessary counseling and outreach.

Consequently, we believe that there is a network now available to do the kind of mortgage lending that needs to be done proactively in those neighborhoods. And the issue for us is:

How can we develop and access that network to do just that?

I'm glad you brought that up. We think it's very, very important.

Senator **D'Amato**. Mr. Herrmann.

Mr. HERRMANN. Senator D'Amato, I grew up in Chicago, so I was there.

Senator DIXON. Well, you grew up in a great City, Mr. Herrmann. You're to be congratulated. [Laughter.]

Mr. HERRMANN. I was there when redlining really came about back in the late 1960's. And I, too, would agree with Ms. Fitts, that greenlining is part of the answer. But, in my judgment, I think those trends are underway. I think what has happened in the last five years or so with respect to fundamental changes in the business of banking have forced bankers, if they like it or not, to see the competitive need here to become more customer-oriented.

And, today, I think many of my other colleagues on the panel might wish to address it, the issue of risk-based capital has now made mortgage lending more attractive for banks.

So we see bankers moving forward aggressively with mortgage lending. It is good business.

Senator D'AMATO. I see time is up and, once again, I want to commend the Chairman for holding these timely hearings. I would hope that, Commissioner Fitts has indicated that we would be able to do more to encourage through the FHA and other programs the kind of greenlining that institutions should be undertaking, particularly as it relates to our urban centers.

I think it's absolutely important. I think it's critical. I think it makes good economic sense and it meets the call of justice providing people with an opportunity for home ownership, making that a reality and not just a myth and something that cannot be attained.

Thank you, Mr. Chairman.

Senator DIXON. I thank the distinguished Senator from New York. May I say that the Chair sees what time it is and we're going to have to go on to the Community Advocacy Groups.

I want to thank this panel very much for taking the time to be with us this morning, and make this observation, if I may.

This Senator certainly doesn't think banks are eleemosynary institutions. They are profit institutions. They have a right to make a decent profit; we want them to. And at the same time, I think that there are corresponding obligations out there among financial institutions to do the right things in lending practices.

That's what we're trying to determine here. With the cooperation of the chairman of the committee, I would say to you that I hope to have another hearing in the spring to pursue this question again in view of the data you are now all gathering, and in view of the fact that I hear from all of you—in some cases, a little vague—ideas about what you're going to do to direct the attention of your particular regulatory agency to the problem we all know exists out there.

So there's going to be another hearing in the spring. I put you on notice, in say March or April. I would hope nobody comes in then and says, well, we didn't know because I put you on notice now—we're going to ask you what you've done to expand the way in which you can get this information, bring this raw data together in a degree of specificity comparing the situations, to demonstrate what the problem is out there for us.

And I would also say to you I'm going to write you each a letter asking your comments first on what you think we can do about this problem—some of the things, Mr. Fiechter, you and others are doing now, other things you've all suggested you might do.

What do you think we can do about the problem, one.

Second, what do you think of mortgage review boards on a voluntary basis where your agency has worked with the institutions you regulate, mortgage review boards where these community advocacy groups or the consumer groups can meet with the financial institutions in these communities to talk about the problems at the community level. You see, without having a lot of bureaucracy involved, that is good old jaw-boning that people can do talking to one another. Mortgage review boards.

Also, tell us more about consumer compliance examiners separate from safety and soundness examiners. Or, if you think, as Mr. Herrmann does, in some cases—maybe not separate examiners—how you think it ought to be done so we're really looking at this separate from the safety and soundness question.

And then, last, answer the question of do we have to go so far as to do testers? You know, that was a very contentious thing. My colleagues here remember how long we dealt with that question of doing testers on the sale and the rental of housing, and we finally came to the conclusion that there was no other alternative. I don't like to see government getting into all these things. None of my colleagues do. But, is that finally the only solution?

Because these statistics—2, 3, 4 to 1—you know, there's something out there that's happening which we've got to correct.

And I want to thank you all. And I know you've all come here in the spirit of good public servants who want to do this, and we want to do it. And we mean it.

So we're not here to hold a hearing and wave the flag; we're here to do something. We're here to see in a couple of years that these statistics change. That's what we want to do. We will pursue it assiduously and I will be back with you in the spring.

God bless you all. Thank you.

The Community Advocacy Groups, Mr. Allen J. Fishbein, Wade Henderson and Stephen M. Dane, Dr. Arthur Johnson and Bernard Parker, and Shanna Smith. Would you all come up here, please?

Ladies and gentlemen, may I tell you what I understand the situation will be with respect to the Community Advocacy Groups?

As I understand it, Mr. Allen Fishbein will testify. Then, as I understand it, Mr. Wade Henderson and Mr. Stephen M. Dane will testify with the understanding that they will divide their 7 minutes however they care to. Dr. Arthur Johnson and Bernard Parker will testify with the understanding they will divide their seven minutes in any way they wish. And Ms. Smith will testify.

May I say that the distinguished chairman of the committee, who has done so many important things in this field, has an obligation almost right now to be with the Majority Leader on a matter of great importance and has sat here very patiently and has asked me, as I will, to indulge him by recognizing Dr. Arthur Johnson and Bernard Parker first in view of the fact that he will have to depart before we hear the entire panel.

I ask everybody to indulge the Chair in doing that, and we'll recognize Dr. Arthur Johnson and Bernard Parker. They are cochairman of the Ad Hoc Coalition on Fair Banking Practices in Detroit. Dr. Johnson and Mr. Parker, we are delighted to see you, sirs.

Senator **Riegle**. Mr. Chairman, if I may, I appreciate your courtesy greatly in calling on these two witnesses first. In addition to the words of introduction that I stated at the outset of the hearing, I wanted to say that these are two very distinguished witnesses we have here, and individuals that I admire greatly for their leadership.

They have an important story to tell, and I'm particularly pleased that they're here in this committee room in the presence of this chairman and this chairman to tell their story today.

ARTHUR JOHNSON AND BERNARD PARKER, COCHAIRMEN OF THE AD HOC COALITION ON FAIR BANKING PRACTICES, DETROIT, MI

Mr. **Parker**. Thank you very much, Senator. And we are pleased to be here to talk about loan discrimination. And we think we do have a story to tell, in Detroit.

First, a little background. Detroit has been a prime example of disinvestment and discrimination in the past. We have lost over 50 percent of our businesses and 40 percent of our population in a 30-year period. And a lot of that had to do with the banking community not being responsive to the needs of the community.

In the seventies, we had a lot of discussion about redlining and anti-redlining laws were passed in Michigan. And many of them were very successful in bringing attention to that. And we think that redlining has resulted. . .

When it went into a new form, a new format of discrimination, one that now terms like "poor credit history, low appraisal value for the homes, poor employment history," and other terms like that became the reason why people were not being able to receive home mortgages.

And we think that when the Free Press did come out with a study last year and they indicated that the difference in racial home mortgages 3 to 1 white to black and in the suburbs 45 to 1 were indications that the feelings people had had were a reality that they were not receiving mortgages as they should.

And particularly when the study showed that Detroiters made up 25 percent of those depositors to those banks, but yet only received about 5 percent of those loans, it became very alarming to us.

In the public hearings that we had where we had regular citizens to come forward, many of them testified to that fact, that a particular person that was making $32,000 a year came in to receive a mortgage at two different banks and she was turned down.

And her comment was, "They make me feel like I was wasting my time. Like I wasn't worthy of being a home owner."

She finally did receive a mortgage from a Chicago mortgage company. But we think that type of indication and others that testified, one indicating that he went in for a mortgage for a second home for $22,000 after paying off his first mortgage, he was denied that mortgage, but later came back within 60 days and received a car loan for $30,000 for a Mercedes Benz.

And that is the perception that many people in our community had toward the financial institutions, is that they were not there to meet their particular needs. And we think that when we came together with the banks, we did not try to harp on that path, what had taken place, but talked about the future and what we expressed to them is two things that we would like to say to the committee here. And both of them are very difficult to put down in some regulatory terms, but it's perception.

It's the perception of what the community feels about the banking industry and that that needs to change, that the banks cannot just sit back and say, well, we are not discriminating more, our codes or process are all equal, but rather they're going to have to go out and try to change the perception of the community so that they then recognize there is not discrimination taking place, so people can take advantage of that.

And also the other thing is the intent and results. Most of the regulators here this morning talked about the banks do not intend to discriminate. And we recognize that. They have put in a process that they would not do that.

But they need to evaluate them on the results. How many loans are they really giving to the minority community? How many loans are people being—are taken advantage of?

And that is the basis the evaluation should be on and not the intent of the bank of discrimination.

We think we were successful in doing this in negotiations with the bank and making them aware of these. And we hope in the future that Detroiters will all be able to take advantage of the products that the bank has.

Dr. Johnson is going to continue on with some of the successes in that area.

Senator DIXON. Thank you.

Dr. Johnson.

Dr. JOHNSON. First, Mr. Chairman, I want to express my genuine gratitude for this opportunity. And then I want very sincerely to express to you, Senator Riegle, and to you, Senator Dixon, who, along with the other members of this committee, have expressed your conscience today about this problem. We are grateful for that and find it encouraging.

I want to say just a few words about our experience as a coalition in Detroit working with the seven banks.

When we met with the leaders of the seven banks in Detroit, we set out to underscore a number of things, but three principal concerns in particular:

One, that mortgage and home improvement lending practices of the banks were having harmful effects on blacks, Detroit neighborhood and the city as a whole.

Two, that Detroit banks were not participating in major development projects at a level consistent with their resources and obligations to the city under the law.

Three, that the changes and remedies we were seeking would have the desirable benefit of bringing about a fundamental change for the better in the relations of Detroit banks, the city and its residents.

I am pleased to report to you today that the seven Detroit banks with which we began negotiations in September of last year have entered into agreements with the Coalition committing $2.7 billion over the next 3-year period in the six key areas of the Coalition's recommendations.

I believe it is much to the credit of Detroit banking leaders and an aroused community leadership in Detroit that these agreements, the last of which was concluded in February of this year, were put in motion without excessive conflict and tensions.

And while the process of getting from the beginning point to the signing of the agreements was not at all easy, there was always enough mutual respect to make the final products possible.

Each of the separate agreements calls for regular meetings between bank leaders and Coalition representatives for the purpose of monitoring and evaluating the bank's progress. These meetings have provided encouraging evidence of the seriousness of our joint efforts.

We must emphasize, however, that the changes we seek together have just begun and the prize is not yet in hand.

The city of Detroit has been hurt badly and unnecessarily so by the greed, callous and racist attitudes of the many who have contributed to the disinvestment patterns of this modern day tragedy.

And, Mr. Chairman, Senator Riegle, I would just cite that, in our city, looking at the effects on neighborhoods at some of what has occurred there, we have announced in the last year by the leadership of the Catholic Church plans to close 31 parishes.

No other American city at any time in our history has suffered such an experience, and it is a threat to the world being evolved.

Here, State and Federal Government bear a large part of the blame for the problems afflicting not only Detroit but virtually every major urban center in the Nation.

We, therefore, recommend to this committee the following:

One, set stricter standards of compliance by banks in meeting community reinvestment obligations. And, like you, I have been discomforted today by the fact that no single individual representing the Federal Government in the regulatory agencies here today could speak with any certainty, with any firmness and insight about the realities of this problem and the practices that we're talking about. That is shameful and it should not be tolerated.

Two, require the collection and periodic analysis of relevant data relating to race, the poor and the cities as seen in the practices of local banks.

Three, more direct and substantial financial aid measures should be adopted to support growth and development in our core cities.

In closing, I want to share with this committee the deeply troubling concern that in every aspect of what we are talking about today there is the problem of race and race relations. In the Detroit area and throughout the Nation.

There is much, far too much that is yet going wrong in America's treatment of racial minorities. Our cities cannot largely be inhabited by the poor and black, largely an impoverished community, and still be expected to preserve themselves in good health.

And if our cities are not healthy, the outer regions will ultimately bear the same burdens and scars.

Thank you for your consideration.

Senator DIXON. Well, I thank you, Dr. Johnson, and you, Mr. Parker, and I wonder whether my colleague, before he's obligated to leave, has anything further.

Senator RIEGLE. Well, Mr. Chairman, we have just heard some very powerful testimony.

And I think the $2.7 billion package of agreements, is very significant in terms of what it can accomplish in the future as it is implemented.

However, I think it's another way of saying that by reaching this consent back and forth, that that is an acknowledgment of the shortfall in the past.

And I think part of the testimony today is that we now have an enormous job of catch-up to do because of patterns and practices that were in place in the past. So now, while affirmative plans are being developed, particularly in Detroit—I think it's important f other urban centers with equivalent patterns to send their people to Detroit and take a look at what's been done there, and initiate local actions on that same order.

That has to be very forcefully supported and driven by actions that we take here under the leadership of you, Senator Dixon, in this committee.

In that respect, what we have put in the savings and loan reform package, it's a big bill. There's a lot in there. And some things got the focus and some things didn't.

Some of the things that didn't get the focus are some of the most important things that are in the bill, going directly at this problem.

We had a train coming through and we put some cars on that train that needed to make their way on through. So I think, as those new elements of the law really start up, they're going to have a very important impact in terms of speeding up the remedy that we have here.

Just one other observation. Most of the hearing is centered on home mortgage lending and home improvement loans which are such a critical part of whether or not a community can hold itself together, maintain itself, thrive, invest in itself and improve the quality of the life of the community.

But there's a very important point made by Mr. Johnson and Mr. Parker with respect to investments in economic development activity over and beyond just mortgage lending. If we don't have a strong economic, commercial and job base, then the whole question of the viability of families and workers is put into jeopardy.

So, we have to look at both things. We have to look at community investment from the point of view of individual lending for things like home mortgages and car loans and things of that kind. But we also have to look at whether or not the basic economic viability of the community as a whole is being fostered and preserved.

This is particularly important when such a large part of the asset base, the depositor base, comes right out of the community itself.

And this is good business. I mean, let it be understood that this is not something that has to do with somehow violating the laws of economics. This has to do with making sure the laws of economics have a chance to work. And when they do, cities thrive.

We think we're demonstrating that in Detroit and we hope other cities will take a look at that and see if perhaps they can follow some of that lead as well.

I thank the Chairman for his indulgence, and particularly the witness—and all witnesses here.

[The complete prepared statements of Bernard Parker and Arthur Johnson follow:]

TO
SUBCOMMITTEE ON CONSUMER AND
REGULATORY AFFAIRS OF THE SENATE
BANKING COMMITTEE
TUESDAY OCTOBER 24, 1989
DIRKSEN SENATE OFFICE BUILDING

FROM: Bernard Parker, Jr.
Operation Get Down

Co-Chair
Ad Hoc Coalition on Fair
Banking Practices in
Detroit

My name is Bernard Parker,Jr. I am Co-chair of the "Ad Hoc Coalition for Fair Banking in Detroit."

We are a coalition of 33 civil rights, religious and community organizations that came together in July 1988 to address the dis-investment of financial institutions in the Detroit community. Since that time, we have been successful in sighing agreements with six (6) financial institutions to reinvestment over 1 Billion dollars in specific targeted areas:

1. **Mortgages**
2. **Home Improvements and**
3. **Small Business and Commercial Development**

We have an overall commitment of 2.7 Billion to be spent in the Detroit community. The perception remains however that Detroit's financial institutions discriminateo against Detroiters and particularly African American Detroiters.

In July 1988, the Detroit Free Press, a major newspaper in the Detroit area, published a series called **"The Race for Money"** which proved there was discrimination and disinvestment by the banks in Detroit.

The research conducted by Hubert H. Humphrey Institute of Public Affairs at the University of Minnesota, found a distinct racial pattern in mortgages and other loans.

SOME BLARING FACTS OF THE RESEARCH WERE:

I. In two (2) comparable neighborhood (one black and one white of equal income and housing stock) the ratio of white mortgages to black mortgages was an average of 3 to 1.

II. Although Detroit represents as high as 25% of the depositors, less than 5% of the loans were to Detroiters.

III. Profiles on Black Detroiters demonstrated that they were more likely to receive a loan from a Saving and Loan or a bank outside of Detroit than from one in the Detroit community.

One person earning $32,000. was turned down by two (2) banks and commented "They made me feel like I was wasting my time, like I wasn't worthy of being a home owner," she finally received a loan from a Chicago Mortgage Company following the advice of her real estate agency.

At least five (5) people testified that they applied for a mortgage and were denied due to poor credit but within a year, received a Automobile Loan. One Black woman that applied for a $22,000 mortgage for a second home, having paid off her first mortgage, was denied the mortgage, how ever, when she later went back to that same bank, she received a car loan of $33,000 for a Mrrcedes BenZ.

The banks used a variety of methods in discouraging and disqualifying individuals for loans i.e.

*Not advertising in black communities or through black radio and newspapers.

*More reception to a car loan than a home mortgage

*Employment appraiser that had little knowledge or concern for the Detroit residents.

*Lack of black employees in the banks, particularly in the Loan Department

*Little communication with neighborhood and civil rights groups.

More black Detroiters felt that banks were not there to meet their loan needs but rather to enjoy the use of their savings and checking accounts.

RECOMMENDATIONS

1. Banks should be evaluated on loan outcomes, not on intends of nondiscrimination banking procedures
2. Statistics should be kept on what percentage of minority applicants are approved.
3. The rating of the banks should be made public.
4. Banks should establish a neutral review committee to reconsider denied loan applicants.

Statement by Arthur L. Johnson, President, Detroit Branch NAACP and Co-chairman, Ad Hoc Coalition on Fair Banking Practices in Detroit before the Subcommittee on Consumer and Regulatory Affairs of the Senate Banking Committee, Tuesday, October 24, 1989 at 10:00 a.m., Dirksen Senate Office Building.

MY NAME IS ARTHUR L. JOHNSON, I HAVE BEEN A RESIDENT OF THE CITY OF DETROIT FOR THE PAST 39 YEARS. I AM COMING BEFORE THE SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS OF THE SENATE BANKING COMMITTEE TODAY IN MY ROLES AS PRESIDENT OF THE DETROIT BRANCH OF THE NATIONAL ASSOCIATION FOR THE ADVANCEMENT OF COLORED PEOPLE (NAACP) AND CO-CHAIRMAN OF THE AD HOC COALITION ON FAIR BANKING PRACTICES IN DETROIT, AND I WANT TO THANK THE COMMITTEE FOR THIS OPPORTUNITY.

IT WOULD BE DIFFICULT FOR US TO BRING BEFORE THIS COMMITTEE MORE TELLING AND DISTURBING EVIDENCE OF PATTERNS OF RACIAL DISCRIMINATION AND DISPARATE EFFECTS AS A RESULT OF PAST BANKING PRACTICES IN THE CITY OF DETROIT THAN WHAT WAS REVEALED IN A SERIES OF INVESTIGATIVE REPORTS BY THE DETROIT FREE PRESS OVER SEVERAL DAYS IN JULY OF LAST YEAR. THE DETROIT FREE PRESS INVESTIGATION DID NOT ESSENTIALLY EXPOSE A NEW EXISTENCE OF UNDESIRABLE RACIAL PATTERNS CONNECTED WITH BANKING PRACTICES IN DETROIT. HOWEVER, IN ITS SCOPE AND DEPTH, IT WAS THE MOST SIGNIFICANT INVESTIGATIVE REPORT ON THE PROBLEMS OF RACE AND THE CITY BY THE DETROIT FREE PRESS THAT I HAD SEEN IN MY 39 YEARS OF RESIDENCY IN DETROIT.

THE EVIDENCE OF THIS SERIES, THE CHRONIC COMPLAINTS THAT BLACK CITIZENS HAD ABOUT MORTGAGE LOANS, AND THE STARK EVIDENCE OF ECONOMIC DISINVESTMENT PATTERNS EFFECTING THE CITY OF DETROIT, WE KNEW WE HAD TO ACT AS A COMMUNITY TO CORRECT THE EXISTING SITUATION. IN LATE JULY LAST YEAR, AS PRESIDENT OF THE DETROIT BRANCH NAACP, I CALLED TOGETHER APPROXIMATELY 140 COMMUNITY LEADERS, AND THE RESULT, AS MY CO-CHAIR, BERNARD PARKER, HAS STATED, WAS THE ESTABLISHMENT OF THE AD HOC COALITION ON FAIR BANKING PRACTICES IN DETROIT.

WITH THE ASSISTANCE OF THE THEN CHAIRMAN AND PRESIDENT OF NEW DETROIT, OUR URBAN COALITION, WE ARRANGED TO MEET WITH THE LEADERS OF 7 OF DETROIT'S

FULL-SERVICE COMMERCIAL BANKS AND 2 SAVINGS AND LOAN ASSOCIATIONS. WE UNDERSCORED IN OUR PRESENTATION THREE PRINCIPLE CONCERNS:

1) THAT MORTGAGE AND HOME IMPROVEMENT LENDING PRACTICES OF THE BANKS WERE HAVING HARMFUL EFFECTS ON BLACKS, DETROIT NEIGHBORHOODS, AND THE CITY AS A WHOLE;
2) THAT DETROIT BANKS WERE NOT PARTICIPATING IN MAJOR DEVELOPMENT PROJECTS AT A LEVEL CONSISTENT WITH THEIR RESOURCES OBLIGATIONS TO THE CITY UNDER THE LAW.
3) THAT THE CHANGES AND REMEDIES WE WERE SEEKING WOULD HAVE THE DESIRABLE BENEFIT OF BRINGING ABOUT A FUNDAMENTAL CHANGE FOR THE BETTER IN THE IN THE RELATIONS OF THE DETROIT BANKS, THE CITY OF DETROIT AND ITS RESIDENTS.

I AM PLEASED TO REPORT TO YOU TODAY THAT THE 7 DETROIT BANKS WITH WHICH WE BEGAN NEGOTIATIONS IN SEPTEMBER OF LAST YEAR HAVE ENTERED INTO AGREEMENTS WITH THE COALITION COMMITTING 2.7 BILLION DOLLARS OVER THE NEXT THREE YEAR PERIOD IN THE SIX KEY AREAS OF THE COALITIONS' RECOMMENDATIONS. I BELIEVE IT IS MUCH TO THE CREDIT OF DETROIT BANKING LEADERS AND AN AROUSED COMMUNITY LEADERSHIP IN DETROIT THAT THESE AGREEMENTS, THE LAST OF WHICH WAS CONCLUDED IN FEBRUARY OF THIS YEAR, WERE PUT IN MOTION WITHOUT EXCESSIVE CONFLICT AND TENSIONS, AND WHILE THE PROCESS OF GETTING FROM THE BEGINNING POINT TO THE SIGNING OF THE AGREEMENTS WAS NOT AT ALL EASY, THERE WAS ALWAYS ENOUGH MUTUAL RESPECT TO MAKE THE FINAL PRODUCTS POSSIBLE.

EACH OF THE SEPARATE AGREEMENTS CALLS FOR REGULAR MEETINGS BETWEEN BANK LEADERS AND COALITION REPRESENTATIVES FOR THE PURPOSE OF MONITORING AND EVALUATING THE BANKS' PROGRESS. THESE MEETINGS HAVE PROVIDED ENCOURAGING EVIDENCE OF THE SERIOUSNESS OF OUR JOINT EFFORTS.

WE MUST EMPHASIZE, HOWEVER, THAT THE CHANGES WE SEEK TOGETHER HAVE JUST BEGUN AND THE PRIZE IS NOT YET IN HAND. THE CITY OF DETROIT HAS BEEN HURT BADLY, AND UNNECESSARILY SO, BY THE GREED, CALLOUS AND RACIST ATTITUDES OF THE MANY WHO HAVE CONTRIBUTED TO THE DISINVESTMENT PATTERNS IN THIS MODERN DAY TRAGEDY. HERE, STATE AND FEDERAL GOVERNMENT BEAR A LARGE PART OF THE BLAME FOR THE PROBLEMS AFFLICITING NOT ONLY DETROIT, BUT VIRTUALLY EVERY MAJOR URBAN CENTER IN THE NATION.

WE THEREFORE, RECOMMEND TO THIS COMMITTEE THE FOLLOWING:

1) SET STRICTER STANDARDS OF COMPLIANCE BY BANKS IN MEETING COMMUNITY RE-INVESTMENT OBLIGATIONS.
2) REQUIRE THE COLLECTION AND PERIODIC ANALYSIS OF RELEVANT DATA RELATING TO RACE, THE POOR, AND THE CITIES AS SEEN IN THE PRACTICES OF LOCAL BANKS.
3) MORE DIRECT AND SUBSTANTIAL FINANCIAL AID MEASURES SHOULD BE ADOPTED TO SUPPORT GROWTH AND DEVELOPMENT IN OUR CORE CITIES.

IN CLOSING, I WANT TO SHARE WITH THIS COMMITTEE THE DEEPLY TROUBLING CONCERN THAT IN EVERY ASPECT OF WHAT WE ARE TALKING ABOUT TODAY THERE IS THE PROBLEM OF RACE AND RACE RELATIONS IN OUR REGION AND THROUGHOUT THE NATION. THERE IS MUCH, FAR TOO MUCH, THAT IS YET GOING WRONG IN AMERICA'S TREATMENT OF RACIAL MINORITIES. OUR CITIES CANNOT BE LARGELY INHABITED BY THE POOR AND BLACK, AND STILL EXPECTED TO PRESERVE THEMSELVES IN GOOD HEALTH; AND IF OUR CITIES ARE NOT HEALTHY, THE OUTER REGIONS WILL ULTIMATELY BEAR THE SAME BURDENS AND SCARS.

THANK YOU FOR YOUR ATTENTION.

Senator DIXON. Well, I thank the distinguished chairman of the committee for his observations.

Thank you very much.

Now, Ms. Smith, would it be your pleasure to go first among the remaining or last? I honored Ms. Fitts' request and I'll do the same for you.

Ms. SMITH. I'd prefer to be last.

Senator DIXON. Thank you.

Mr. FISHBEIN. Mr. Allen Fishbein, general counsel, Center for Community Change.

ALLEN J. FISHBEIN, GENERAL COUNSEL, CENTER FOR COMMUNITY CHANGE, WASHINGTON, DC

Mr. FISHBEIN. Thank you, Mr. Chairman. I want to thank the subcommittee and commend it on holding these hearings; I think they're very timely and very necessary.

My organization is a national nonprofit group that provides technical assistance to low-income and minority community groups in the area of community reinvestment and fair lending.

And I brought a number of attachments with me today that I made reference to in my written testimony, Mr. Chairman, and I would appreciate it if you would allow me to insert them in the record.

Senator DIXON. That will be done.

Mr. FISHBEIN. OK. Thank you.

It's been more than 20 years since the enactment of the Fair Housing Act. And what we've been seeing in recent years is that there is a growing body of research that indicates that racial factors affect the supply of mortgage credit in many cities in this country.

My own organization published a study last June using home mortgage disclosure data. We assembled one of the largest data bases of its kind. We looked at two years worth of lending by banks, S&L's and credit unions in 14 major cities. It encompassed a half a million loans.

We estimate the data base is about 15 percent of all the census tracts in the United States. And what we found is that the rate of mortgage lending in minority communities was one-third of what it is in nonminority communities. The rate, meaning the number of loans per 1,000 owner-occupied dwelling units.

Moreover, we found that this differential continues regardless of income level, so that in a middle income census tracts comparing minority and nonminority, the difference is still one-third lending. And it doesn't seem to be related to income.

Other research has highlighted the same thing. There was reference in the earlier panel to the Federal Reserve Bank of Boston's study. The bank itself studied mortgage lending activities in the city. It did everything it could to try to explain the differences that there were between lending in minority and nonminority neighborhoods.

When the Fed considered all factors, race seemed to stand as an isolated factor and explained the differential in lending.

The Atlanta Journal Constitution in 1989 obtained data from the Federal Home Loan Bank System which found that the loan rejection rates for individuals who were minorities for the home purchase loans was uniformly twice as high as it was for nonminorities. For example, the rejection vote in the city of Chicago was four times higher for minorities than non-minorities. In Detroit, almost four times higher.

I think the reason that we're seeing these differentials, and this is a key part of my testimony here today, is that the banking regulatory agencies that have had this responsibility for 20 years just simply lack the will or the expertise to determine whether discrimination is occurring.

As you have seen their response to this research is to treat it as a marketing issue, to basically say the problem alone is that the banks aren't marketing credit actively enough in minority neighborhoods.

Perhaps that is part of the problem. I think it is too facile an explanation to say that it is all of the problem.

They also talk about the fact that their examination reports do not find—what they call overt—discrimination.

Well, there is another problem area besides marketing; it exists somewhere between marketing and overt discrimination. There can be discrimination for unintentional reasons. There can be loan policies in place that have an unintentional effect of discriminating against certain classifications of people. And I think that may be part of the problem.

Senator DIXON. Can you give me an example of that, Mr. Fishbein?

Mr. FISHBEIN. Well, I will give you an example. Many institutions are starting to use minimum loan size requirements for mortgage loans in which you cannot apply to the institution for mortgage loan unless you are applying for excess of $20,000-30,000. And when you look at the housing stock in a particular community, it may mean that a very large percentage of the minority population lives in housing below that amount.

Senator DIXON. I see.

Mr. FISHBEIN. So, in effect, a policy that appears neutral on its face may have the effect of discriminating against minorities in a particular community.

Senator DIXON. Thank you.

Mr. FISHBEIN. The so-called "Effects Test" area has probably been one of the least utilized parts of the banking regulatory agencies enforcement program.

Not to make light of the situation, but I think it captures our feeling. In a court of law, you can have a witness declared a hostile witness. This committee ought to declare the banking regulatory agencies hostile witnesses for the purposes of implementing the fair lending laws.

And the reason I say that is it took a lawsuit by the major civil rights organizations in this country just begin to get the banking regulatory agencies to enforce the Fair Housing Act.

Senator DIXON. I might interrupt by saying I don't know that I'd find them hostile, but I don't find them very motivated, I must agree. [Laughter.]

Mr. **FISHBEIN**. I guess reasonable people can disagree on their state of mind. But I think the outcomes speak for themselves.

For example, the Federal Deposit Insurance Corporation, which had set up a computerized analysis system as a result of a settlement to this lawsuit I mentioned, disbanded that analysis system in 1982.

They did it at the same time that they were maintaining that because of other resource constraints they now perform fewer and fewer exams than they could in the past.

So, at the same time that they're performing fewer exams, they have disbanded the one computerized analytical tool that they had which was designed to be cost-effective and make the examiner's job more efficient when they went into the institution.

The Comptroller of the Currency has an approach of using a system-wide compliance approach; rather than finding individual violations of fair lending, they look to see whether the internal Fair Lending program that an institution has in place is adequate or not.

And that may be one of the reasons that they find very few substantive violations of the Fair Housing Act.

Senator **DIXON**. As a matter of fact, they said they found none.

Mr. **FISHBEIN**. If you look over the past 10 years, there have been virtually no referrals to the Department of Justice of violations for prosecution under the Fair Housing Act. I think that is probably the most damning evidence of them all.

Now, in terms of recommendations and I set this out in my written testimony, first and foremost, we really encourage this committee to have an agency of the federal government sponsor a testing program for lending discrimination. I think the representative from the Comptroller's Office acknowledged that one of the areas that they clearly do not even make a pretense at being able to detect is possible discriminatory practices at the pre-application stage, when an inquiry is made of an institution and perhaps a minority applicant is discouraged.

Now, testing is using matched pairs of people who are identical in all respects except one is minority and one is non minority. Testing is used to determine whether there's differential treatment in the mortgage lending process.

We have been part of an experimental program with two State governments that has done that and we think we have learned quite a bit about it.

And we have also found what we think——

Senator **DIXON**. What States?

Mr. **FISHBEIN**. I'm not at liberty to disclose because we were in the role of consultants and it really is for those two ——

Senator **DIXON**. Could you to us privately? Could you see if you could to us privately?

Mr. **FISHBEIN**. Yes, I certainly can.

Senator **DIXON**. Thank you.

Mr. **FISHBEIN**. And what we found is that there was differential treatment at the pre-application stage. It was that the loan officers in a number of cases would provide information to nonminorities, to white testers that they would not provide to minority testers which would help them qualify for a loan.

And it suggests that more systematic use of testing might help address some of those differential rejection rates that we were talking about before.

Second, the Federal Home Loan Bank System, now the Office of Thrift Supervision, for over 10 years has had a nondiscrimination regulation in place, which specifically makes red-lining illegal and it requires S&L's to publish their loan underwriting standards so the public can come in and inspect them. And so examiners can determine whether individual lenders are adhering to their policy.

They are the only one of the banking agencies to have such nondiscrimination regulation in place. That is significant because what, in effect, the banking regulators have to do when they go in to examine is they have to determine what that loan underwriting policy is based on conversations with bank personnel, or perhaps based on reviewing some sampling of loan files.

And that having written policies in place which they then could review the files against would be a much more effective way of ensuring adequate compliance.

Third, and it was mentioned by some of the members of this subcommittee in questioning, we have long believed that separate divisions with Consumer Affairs Lending and CRA examiner specialists is absolutely crucial to an effective enforcement.

None of the agencies have separate divisions that report directly to the chief of the regulatory agency.

The Federal Reserve Board comes closest. They have a Consumer Division, but that division does not get a chance to report directly to the Board on expansion applications that are being considered. We think each one of these agencies ought to have separate divisions with separate career paths and recruit people who will become specialists in enforcing this very important part of the law.

In closing, I think the dilemma we have had, Mr. Chairman, is that no matter what enforcement tools we come up with, there is still the lack of will on the part of these regulatory agencies to effectively implement them.

And, therefore, as a final suggestion, we urge the Subcommittee to instruct the General Accounting Office to undertake a study of the effectiveness of the existing Fair Lending Programs and to consider whether transferring this authority, this responsibility, to a single agency—perhaps a nonbanking regulatory agency—in order to provide an improvement in overall enforcement.

Thank you very much.

[The complete prepared statement of Allen Fishbein follows:]

center for community change

TESTIMONY BY

ALLEN FISHBEIN
GENERAL COUNSEL

CENTER FOR COMMUNITY CHANGE

WASHINGTON, DC

ON

MORTGAGE LENDING DISCRIMINATION AND FAIR LENDING ENFORCEMENT

BEFORE

THE SUBCOMMITEE ON CONSUMER AND REGULATORY AFFAIRS
COMMITTEE ON BANKING, HOUSING AND CONSUMER AFFAIRS

UNITED STATES SENATE

OCTOBER 24, 1989

Good morning, Mr. Chairman, and members of the Subcommittee on Consumer and Regulatory Affairs. My name is Allen J. Fishbein and I am General Counsel of the Center for Community Change and Director of the Center's Neighborhood Revitalization Project. The preparation of my written testimony was assisted by Elizabeth Hamill, Shriver Peace Worker, who is the Project's Research Assistant.

The Center for Community Change (CCC) is a national non-profit organization, based here in Washington, DC, which provides research and technical assistance to community-based organizations representing low income and minority areas. We focus primarily on issues concerning neighborhood revitalization, community reinvestment, and lending discrimination. Our publications include the CRA Reporter, which features stories on community reinvestment activities. CCC also monitors the federal banking regulatory agencies enforcement of the Community Reinvestment Act, the Home Mortgage Disclosure Act, and the fair lending laws.

Our recent work in the fair lending field is several fold. At the present time, we are advising several state human rights agencies on a demonstration project designed to detect incidences of mortgage lending discrimination, through the use of testing.

In addition, we recently published a major study which, among other things, compared mortgage lending activity in minority and non-minority neighborhoods in fourteen cities.

Mr. Chairman, we commend you for holding these hearings on mortgage lending discrimination. They could not be more timely. Although it has been more than twenty years since the passage of the landmark Fair Housing Act, which made it unlawful for mortgage lenders to discriminate, a growing body of research strongly indicates that racial factors continue to influence the flow of mortgage credit in our nation's cities.

Unfortunately, the four federal banking regulatory agencies with fair lending enforcement responsibilities for banks and thrifts -- Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, Office of Thrift Supervision (formerly the Federal Home Loan Bank Board), and the Federal Reserve Board -- this research has had hardly any apparent impact. All apparent signs indicate that these agencies are either unable or unwilling to use the full scope of their supervisory powers to address the problem of mortgage lending discrimination. Their failure to upgrade their enforcement programs in the face of these recent findings is resulting in a crisis of confidence about their ability to handle the job. Based on previous experience, the regulatory agencies performance is unlikely to improve in any signficant way without strong congressional prompting. In my testimony today, I will make a number of recommendations on how we believe that enforcement can be strengthened.

I am sure that the Subcommittee agrees that achievement of fair lending practices must be a vital objective of public policy. Accordingly, three fundamental questions posed by these oversight hearings: 1) Is there evidence that mortgage lending discrimination is a significant problem? 2) Are current fair lending laws being adequately enforced? 3) If not, what changes are needed? We urge the Subcommittee to investigate these issues thoroughly.

1. Evidence Indicates That Mortgage Lending Discrimination Remains A Problem

There is a common belief among many in the lending industry that discrimination does not occur anymore. After all, they will tell you, it is against the law and also that it is the market and not peoples prejudices that determines where the money flows. However, this view conveniently ignores the discriminatory legacy of the past. One well known lending discrimination expert described that legacy this way:

> For over hundred years, reflecting the social and legal tone of national life, discrimination in housing was interwoven and institutionalized in every aspect of real estate transactions, including mortgage lending, as a 'natural,' and therefore appropriate, function. Not only was discrimination integral to the industry, but people who were serviced by the industry expected it as the way of doing business. The Federal Government encouraged it and the courts upheld it. Greene, Zina,

Lender's Guide to Fair Mortgage Pulicies, The Potomac Institute, Wash, DC, 1980, at 1.

In the 1960s and 70s, Congress enacted two laws to directly prohibt discrimination in mortgage lending -- the Fair Housing Act and the Equal Credit Opportunity Act. These laws, along with the Home Mortgage Disclosure and Community Reinvestment Acts, which focused on redlining and other forms of geographic discrimination, have helped to curb many of the most blatant forms of bias against minorities that were once prevalent in the housing finance industry. However, considerably less progress has been made in combatting many of the more subtle, or even, unintentional forms of discrimination against minorities and the neighborhoods in which they live.

While perhaps this is not the proper time to present an elaborate treatise on mortgage lending discrimination, one example may help to illustrate that the patterns, policies, and practices of over a hundred years of discrimination will not change quickly despite the existance of legislation.

In 1972, four years after enactment of the Fair Housing Act, a Federal Home Loan Bank Board survey of its member institutions found that as many as 30% of the industry actually admitted to using illegal, racially discriminatory lending practices as part of their routine mortgage underwriting.

Apparently, old traditions die hard. A host of statistical research using Home Mortgage Disclosure Act data has been conducted in recent years. These studies show ongoing disparities in the levels of mortgage lending between minority and non-minority neighborhoods for many cities. Most of these studies reached very similar conclusions -- that the racial composition of a neighborhood is a significant factor in determining where mortgages are made or not made.

A. Three Examples of Studies That Reveal Race Affecting Mortgage Lending

In my written testimony today I would like to focus on just three of these studies. A bibliography and summary of a number of the major studies is included as Attachment I.

o S&L's Shun Lower Income and Minority Neighborhoods

A study issued last June by CCC found that, on average, the rate of mortgage lending activity for depository institutions (i.e. loans per 1,000 owner-occupied 1-4 family dwelling unit) was more than three times greater in non-minority census tracts than it was in minority census tracts. Looking at 1986-7 Home Mortgage Disclosure data for fourteen cities (approximately, 15% of all the census tracts in the US), we found that the disparities exist even when the income level of the census tracts is taken into consideration. For example, we found that banks, S&Ls, and credit unions provided mortgages to middle income minority census tracts at a rate that is only 36% of the rate in middle income non-minority census tracts. See Attachment II

o Geographic Patterns of Mortgage Lending in Boston

. This past summer, the Federal Reserve Bank of Boston acknowledged that even its own research had established that race is an important factor in determining the level of mortgage originations in Boston neighborhoods. As part of the study, the Boston Fed analyzed about 48,000 property transactions over a five year period. The study concluded: "Lower mortgage originations in black neighborhood cannot be explained away by lower levels of income and wealth, lower rates of housing development or other neighborhood differences. Even after taking these factors into account, one still finds a substantial discrepancy between mortgage originations relative to the housing stock in white and black neighborhoods. . ." See Attachment III

o Blacks Turned Down for Home Loan From S&Ls Twice As Often As Whites

The Atlanta Journal-Constitution reporter Bill Dedman, who received a Pulitzer Prize for his four-part series on lending discrimination in Atlanta, cracked another story when he obtained data from the Federal Home Loan Bank system indicating that Black mortgage applicants were rejected by S&Ls twice as frequently as Whites, and that other racial minorities were also rejected more frequently as well. His research also found that applicants from high income minority neighborhoods were more likely to be rejected for mortgage credit than those from low-income non-minority neighborhoods. The Dedman report was the first significant study to look at racial characteristics of borrowers of mortgage credit. Prior to the release of this data, researchers were limited to comparing lending patterns to the demographic characteristics of census tracts. The Dedman article concluded that redlining and racial discrimination may have grown worse in the 1980s as federal regulators decreased enforcement of the fair lending laws. See Attachment IV.

These and the other statistical studies raise strong new evidence that problems exist, whether or not they result from illegal activity. Unfortunately, the studies also raise additional doubts about whether current enforcement apparatus is adequate to detect illegal activity and to take the necessary steps to correct the violations.

2. Current Enforcement Is Not Adequate

The regulators response to the findings have been both disappointing and very predictable. For example, the Federal Reserve Board discussed several of these studies in their Report on Loan Discrimination mandated by Section 1220 of FIRREA. The

Fed report states, "The studies, however, do not draw definitive conclusions about the existance or extent of racial discrimination." (Report on Loan Discrimination, Federal Reserve Board, at 19).

Admittedly, it is necessary to interpret the research findings carefully. A number of factors, some of which may be legally prohibited and some which may not, may explain the disparities in lending levels, between otherwise comparable minority and non-minority neighborhoods. For example, the disparities may be attributable to the lack of aggressive marketing by banks and S&Ls in minority neighborhoods. Yet, either intentional or unintentional discrimination may be at least part of the explanation as well or it may result from discrimination, either intentional or unintentional. The point is that under current enforcement procedures it is unlikely the agencies will be able to make this judgment.

In fact, the regulatory agencies have been quick to jump on the lack of marketing theory to explain the disparities. They argue that the low level of lending in minority communities is a Community Reinvestment Act issue rather than a fair lending enforcement issue. By this they mean that to the extent the disparities do not represent legitimate economic factors, they can be addressed simply by encouraging financial institutions to increase their outreach and marketing to underserved minority neighborhoods.

Aside from the obvious questions this posture poses to the effectiveness of their past CRA enforcement efforts, the Fed's response skirts the issue of whether or not discrimination has occurred. Even if we accept the Fed's contention that the research showing disparities is inconclusive, their response neglects to discuss to what extent the results are attributable to loan policies by individual institutions that may have a discriminatory effect on minority applicants. Discrimination is not only a result of deliberate, or invidious, bias against an applicant or neighborhood. It may result from policies and/or practices lenders use that have the effect of denying or restricting the flow of mortgage dollars to minorities or minority neighborhoods.

-- Effects Test Analysis is Underused By the Regulatory Agencies

In fact, the "effects test" is seldom invoked by the banking regulators, although it is used in other areas of civil rights law, such as fair employment. It receives only scant attention in the compliance handbooks and in examiner training.

In the field of credit, for example, a proper analysis would look to whether the lending criteria and practices of the lender have an adverse impact on racial minorities or women. If so, it becomes incumbent upon the lender to demonstrate that the practice serves an overriding business necessity; for example, the practice is required to reduce lending risks to an acceptable level. If that is the case, then the practice is lawful despite its discriminatory impact, unless there is another criterion which might be used by the lender which would have a lesser discriminatory impact but which would equally serve the business necessity of the lender.

Examples in the area of mortgage lending would be a policy of prefering older homes rather than new homes, or perhaps a minimum loan size or lot size requirement. Minority homebuyers are significantly less likely to have previously owned a home, or more likely to be purchasing a smaller sized or less expensive property.

Agency examiners should be looking at underwriting pratices of lenders to determine whether effects test issues arise. Unfortunately, only S&Ls are required to have written mortgage loan policies, so that bank examiners must expend additional time to ascertain these policies. This makes it more difficult for examiners to spot possible effect tests problems.

-- Agencies Using CRA To Avoid Citing Fair Lending Violations

It is understandable that the banking agencies would prefer to soft pedal the implications of the lending disparities the studies are finding. Violations of these two fair lending laws necessitate taking immediate supervisory action (including cease and desist orders) against the institution(s) engaged in prohibited activity. On the other hand, classifying the problem as a "CRA issue" merely requires the regulator to take the information into account as part of a much broader community reinvestment evaluation process. Once the findings are treated as a CRA problem, rather than a fair lending compliance issue, at most it will be used to downgrade a particular lender's CRA rating. Since at last count, only a handful of lenders receive poor CRA ratings in any given year, it is simply inadequate to limit evidence of potential discriminatory practices to a CRA analysis.

Apparently, the US Department of Justice was similarly dissatisfied with the regulatory agencies response to the Atlanta Journal-Constitution's study, since it has undertaken an unprecedented investigation of mortgage lending practices in that city to determine whether violations of law have occurred. But the question remains: why didn't the four banking regulatory agencies undertake a similar type of investigation for the lenders they supervise.

-- Weakness In Enforcement Fits All Too Familiar Pattern

The banking agencies lacklustre response to this latest research, is quite consistent with their past efforts to curb lending discrimination. Quite literally, they have had to be dragged kicking and screaming into performing their civil rights enforcement duties, almost every step of the way.

For almost eight years after passage of the Fair Housing Act, the four banking regulatory agencies did virtually nothing to implement their new enforcement responsibilities. The 1976 oversight hearing conducted by the Senate Banking Committee revealed the extent of the agency inaction and led the then Chairman, Senator William Proxmire to conclude: " . . . I thought the record (of the regulatory agencies) was pretty disgraceful. There was really no effective enforcement of the antiracial discrimination laws." Implementation and Enforcement of Fair Mortgage Lending Laws and Regulation, Hearings before the Committee on Banking, Housing, and Urban Affairs, US Senate, 96th Cong., First Session, 1979, at 1.

Frustrated by the agencies footdragging, in 1976 twelve civil rights organizations sued the four agencies, in National Urban League, et al. v. Comptroller of the Currency, et al. in the US District Court for the District of Columbia (C.A. No. 76-0718). The following year, three of the four agencies entered settlement agreements to settle the lawsuit out of court (the suit against the Federal Reserve Board was dismissed by the court due to lack of standing and no settlement was reached with that agency).

A key element of the settlement agreements was a commitment by the agencies to establish a system for collecting and analyzing race and sex data on home mortgage applicants. The purpose of the system was to identify patterns of potential discrimination at individual lending institutions so that examiners could then go into those institutions and conduct in-depth investigations.

In December 1979, Senator Proxmire held the last oversight hearings on fair lending enforcement until this one. At these hearings, the agencies went to great lengths to explain that they were actively involved in implementing the terms of the settlement agreements, although they admitted that progress was slower than anticipated. Unfortunately, each agency adopted its own approach and procedures to fair lending enforcement, a fact noted in the hearings. Outsiders have often found these differences quite bewildering and it has made oversight in this area particularly difficult.

All of the settlement agreements expired in the early 1980s, and while the plaintiffs to the National Urban League met regularly with the agencies while they were in existance, very little monitoring of fair lending enforcement has occurred in recent years. We do know, however, that the Federal Home Loan Bank Board data analysis system is the last remaining legacy of the lawsuit. Unfortunately, for many years the S&L regulator did not analyze or use the data as a routine part of its enforcement efforts. The OCC maintains a semblance of its original system, while the FDIC dropped its computer analysis system altogether.

The termination of the FDIC's COMPASS system means that individual examiners must perform the time consuming task of determining acceptance and rejection rates for different categories of applicants. Since the FDIC has curtailed it annual on-site examination by about one-half since 1980, it is highly likely that this type of analysis is performed on only limited basis.

Moreover, in the early 1980s overall fair lending enforcement along with other consumer compliance was sharpely curtailed. A study by BankWatch, a well respected research organization, found that the total examiner hours spent on fair lending, consumer compliance and CRA dropped by 74% from 1981-1984.

"Its Deja Vu All Over Again"

Yogi Berra, one of the nation's foremost humorists, is reported to have once said: "Its Deja Vu All Over Again." Yogi's remark came to mind as I was reviewed the reports submitted by the regulatory agencies in response to Section 1220 of the Financial Institutions, Reform, Recovery, and Enforcement Act. The agencies response to inquiries about lending discrimination or their fair lending enforcement efforts suggests this is a new area of responsibility for them and not something they have been required to do for the past twenty years.

Section 1220 required each of the banking regulators and the US Department of Housing and Urban Development to report on their findings on the extent of discriminatory lending practices by mortgage lenders they supervise "based on a review of currently available loan acceptance and rejection statistics." The provision also requests recommendations for new measures to assure nondiscriminatory lending practices.

Although each of the five reports (I did not have an opportunity to review the report submitted by HUD) takes a somewhat different tack, they all have one central feature in common. The reports indicate very clearly that the regulatory agencies do not have any firm sense about the extent to which mortgage lending discrimination exists. In fact, the Office of Thrift Supervision (formerly, the FHLBB) is the only agency to have data on loan acceptances and rejections. The three agencies currently without a system for collecting acceptance and rejection statistics point to the new requirement in FIRREA, which will require mortgage lenders to maintain this type of information beginning in 1990. This is rather ironic, since none of these agencies had supported inclusion of this provision during last year's legislative debate.

However, the most disturbing aspects of these reports is the virtual lack of recognition of the implications of the studies I have discussed earlier. In fact, only one of the reports even refers to the lending studies, although certainly not with any sense of urgency. Accordingly, I guess it is not surprising that their recommendations were quite minor and certainly not calculated to strenthen fair lending enforcement.

The OCC's response to the Section 1220 request was extemely limited, considering it regulates the nation's largest banks. Interestingly, the agency described its Fair Housing Home Loan Data System (FHHLDS), but it chose not to provide any illustrations of the type of analysis that is performed. For example, we obtained data through a Freedom of Information Request from the OCC, which indicated that it was far more likely that minority applicants with a high probability of approval were actually rejected than white applicants with a high probability of approval. This data is comparable to acceptance/rejection statistics.

The agencies recommendation for improvements were very disappointing. The National Credit Union Administration viewed the reporting requirement as frivolous and provided no recommendations at all. The OCC and FDIC indicated that recommendations would be considered by the Federal Financial Institutions Examination Council (FFIEC), which they sit on, but failed to state what these recommendation would be. The Federal Reserve Board listed a series of recommendations that were not very substantial. Although few details were provided, the OTS provided the only substantive recommendations. Its report indicated that the FFIEC was considering the use of "testers" to provide more information to detect pre-screening forms of discrimination, along with a team approach to investigating geographic areas with loan disparities.

In general, the report implied that they did not see new compliance issues emerging as a result of recent developments. According to this view, since their compliance exams consistently turn up few substantive violations, and relatively few discrimination complaints are received from consumers, the industry must be in basic compliance with the law. Of course, the fallacy with this view is that it assumes that "no news is good news," which may not be the case. It also assumes that existing enforcement techniques are adequate for detecting lending discrimination or that more effective procedures cannot be employed.

Only the Federal Reserve Board acknowledged the limitations of its current procedures. State-member banks are not required to maintain written loan policies, and therefore examiners are assigned the difficult tasks in determining whether variations from the norm reflect considerations or are due to illegal discrimination. Moreover, as the Fed's report readily concedes, their compliance examination is not very useful at determining whether minority applicants are being discouraged from submitting an application.

Another weakness in all of the agencies compliance exams are that they tend to rely on the justification provided by a lender for credit denials. Thus, if the reason provided for rejection is that the applicant was not sufficiently creditworthy, examiners seldom have time to determine whether, in fact, this was actually the case. Accordingly, minorities may be denied credit on a differential basis from non-minorities without it coming to the attention of agency examiners.

Nor should the lack of consumer complaints necessarily reflect the lack of lending discrimination. Most applicants are unfamiliar with the mortgage loan process. Indeed, most homebuyers are intimidated by the application procedures and therefore, are unable to determine whether they have been denied credit on a impermissible basis. They tend to accept, passively and unquestioningly the lender's decision -- favorable or adverse -- on loan applications. As a result, homeseekers are less likely to complain to public or even private agencies about wrongful treatment at the hands of mortgage lenders than they are about sales or rental agents.

Not withstanding the complexities involved in the mortgage lending process, experience has demonstrated that where an agency is aggressively challenging mortgage lending practices to disadvantaged minorities, the publicity surrounding the activity will encourage many individuals to step forward with lending complaints. The Toldeo Fair Housing Center is an excellant example of this approach. After bringing a number discrimination lawsuits against local lenders, the private agency received 48 complaints over a one-year period, or more complaints than had been received nationwide by HUD during the same period.

3. Recommendations for Strengthening Enforcement

Immediate steps must be taken to upgrade fair lending enforcement procedures in order to determine the extent to which illegal activity is occurring. We recommend the following steps:

a) HUD Should Initiate A Mortgage Lending Testing Program

Testing is the investigative technique commonly used by fair housing groups and human rights agencies to uncover discriminatory practices in the sales or rental of housing. It is recognized by the courts as a valid means for uncovering discrimination. Matched pairs of loan applicants (minority and non-minority) solicit information or may even apply for a mortgage to determine whether any differential treatment is afforded each. Testing can be an effective means for identifying lenders who pre-screen or otherwise discourage minorities from even filing loan applications.

We have advised several human rights agencies on how to test for mortgage lending discrimination and believe if can be quite effective. Unfortunately, the banking regulatory agencies have resisted the use of testing. Their resistence appears to be mainly attributable to the belief that it complicates their relationships with the institutions they supervise.

Accordingly, we believe that the authority for mortgage lending testing should be assigned to HUD, which has expanded enforcement responsibilities for fair lending as a result of the Fair Housing Act Amendments. HUD Fair Housing and Equal Opportunity Office should be directed to contract with private fair housing agencies to conduct random tests of mortgage lending institutions. The agency should coordinate the testing activities with other relevant supervisory agencies.

b) Nondiscrimination Regulations For S&Ls Should Be Extended To All Mortgage Lenders

Since 1978, the Office of Thrift Supervision has prohibited, among other things, refusals to consider loan applications on the basis of the age or location of the dwelling, and discrimination based race, color, religion, sex, or national origin, in fixing the amount, interest rate, duration, application procedures, or other terms or conditions of housing related loans. These rules operate in addition to the provisions of ECOA, and its implementing regulations. The regulation also prohibits S&Ls from relying on discriminatory appraisal and underwriting standarsds and requires each institution to have written loan underwriting standards, which are available to the public upon request.

Commercial banks are not currently required to adhere to similar types of regulations, although arguably it would be illegal for them to engage in any of these activities. We urge the Subcommittee to instruct the agencies to adopt similar regulations. Moreover, all mortgage companies approved for FHA insurance should be required to adhere to these standards.

c) Establish Separate Consumer Divisions Within Each of the Regulatory Agencies.

As with CRA, fair lending enforcement needs to receive much higher priority within each of the agencies. An important means for ensuring that area is afforded greater weight in the future is to require each agency to establish a separate consumer division.

The separate divison would have responsibility for conducting fair lending, CRA, and consumer compliance examinations using a trained staff of specialists in these areas. The consumer division would also respond to consumer complaints, enforce laws regarding fair lending, consumer protection, and community reinvestment. The head of this division should report directly to the agency head. The division should also make recommendations on pending expansion applications directly to the agency head based on the fair lending/CRA/consumer compliance records of the applicant institutions.

At the present time, only the Federal Reserve Board has a fully separate consumer division. The division does not, however, report directly to the Board on recommendations for action on pending expansion applications.

d) Relief From the Federal Paperwork Reduction Act

Another important step for improving agency enforcement would be to exempt the banking regulatory agencies from the requirements of the Federal Paperwork Reduction Act for information related to fair lending, CRA, and consumer compliance. The act directs the agencies to reduce the reporting and record keeping requirements that they impose on financial institutions.

There appears to be some uncertaintly as to what extent the banking agencies are covered by the act. However, the old FHLBB, OCC, and FDIC have chosen to place key reporting requirements, such as fair lending reporting, under the act's purview. The pressures to cut back on fair lending reporting will intensify as reporting is expanded in other areas, such as safety and soundness. The Paperwork Reduction Act, in effect, creates a "zero-sum" game, in which the agencies endeavor to reduce reporting requirements in the fair lending and consumer compliance areas, as they add safety and soundness reporting requirements, such as expanded Statement of Condition Reports.

e) Small Business Loan Disclosure

As the Home Mortgage Disclosure ACt has unquestionably demonstrated, disclosure of information about lending patterns of financial institutions is an effective means for spotting possible credit discrimination and a relatively low-cost method for encouraging improved lender performance. Requiring depository lenders to report on their small business lending on a census tract basis, or perhaps as a separate item on the State of Condition Reports, would be an important new monitoring mechanism for determining whether banks are discriminating against certain business owners or enterprises located within certain geographic areas.

f) Annual Reporting to Congress.

Each agency should be required to submit more detailed annual reports to Congress on the number of examiner hours devoted to fair lending and CRA compliance for the preceding year. The reports should provide additional details about the violations that are detected and any corrective action taken.

One area we have not made any recommendations is whether or not the banking regulatory agencies fair lending enforcement responsibilities should be transferred to another agency. We urge to Subcommitte to request the US General Accounting Office to undertake a full fledged review of fair lending enforcement and specifically, to make recommendations as to whether transferring the banking agencies enforcement authority to HUD, or another agency is advisable.

Mr. Chairman, this concludes my formal testimony. I will be glad to answer any questions you or the other Subcommitte members might have.

TESTIMONY BY

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WASHINGTON, DC

ON

MORTGAGE LENDING DISCRIMINATION AND FAIR LENDING ENFORCEMENT

BEFORE

THE SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS

UNITED STATES SENATE

OCTOBER 23, 1989

Attachment I

MORTGAGE LENDING STUDIES:

1. CCC. S&L's Shun Lower Income and Minority Neighborhoods. The Center for Community Change, 1989; analysis of 1986 and 1987 HMDA data in fourteen cities representing over 15% of the nations's census tracts.

"...Using HMDA and census data. the research project compared mortgage loan activity in non-minority census tracts with minority census tracts. the data showed that, on average. the rate of mortgage loan activity was more than three times greater in non-minority census tracts than it was in minority census tracts. The disparities between lending activity occur even when the income level of the census tracts is taken into consideration...."

"...in comparison with commercial banks. S&L's on average focus a higher proportion of their mortgage lending efforts in more affluent neighborhoods...."

"...institutions that are non-users of the Federal Home Loan Bank's borrowing window have the highest percentage of their assets in residential mortgages. The percentage of mortgage holdings declines steadily as cash advance use increases...."

2. Bradbury, Katharine L., Case, Karl E., and Dunham, Constance R. Geographic patterns of Mortgage Lending in Boston. The Federal Reserve Bank of Boston, 1989; an analysis of roughly 48,000 real estate transactions from 1982 through 1987 in Boston's 60 neighborhoods.

"...The statistical analysis introduced a number of neighborhood economic and demographic characteristics that could affect either the supply and demand for housing or the supply and demand for mortgages. The results, however, continue to indicate that race is an important factor. Lower mortgage originations in black neighborhood cannot be explained away by lower levels of income and wealth, lower rates of housing development or other neighborhood differences. Even after taking these factors into account, one still finds a substantial discrepancy between mortgage originations relative to the housing stock in white and black neighborhoods..."

3. CREN. Checking out of Hartford: Bank Priorities vs. Neighborhood Needs. The Citizens Research and Education Network 1989; Survey of Hartford area banking services;analysis of the 1987 Commercial Record, 1985-1987 HMDA data, and 1987 data from the Hartford Human Relations Commission

"...The results show that the neighborhood that received fewer than the median number of loans per building are almost exclusively in the North End and Frog Hollow areas, neighborhoods which are largely Black and Hispanic....According to information supplied annually by Hartford banks to the city's Human Relations Commission, in 1987 banks denied Hartford mortgage and home improvement loan applications as much as four times as often as they denies suburban applications. Forty percent of home mortgage applications originating in Hartford's North End were denied, in Hartford as a whole 22%, and in the region only 11%..."

4. Dedman, Bill. "Blacks Turned Down for Home Loans From S&Ls Twice as Often as Whites", The Atlanta Journal-Constitution, 1989; statistics obtained from the HLBB through a FOIA request; analysis of $1 trillion in loan applications.

"...The records of 10 million applications from every savings and loan in the country reveal a lending gap so pervasive and so wide that in much of the country high-income blacks are rejected at the same rate as low income whites.

The loan records suggest that redlining - refusing to lend in an area because of race - has persisted and may have grown worse in the 1980s as federal regulators decreased enforcement of fair lending laws...."

5. Goldstein, Ira J., Ph.D., and Shlay, Anne B., Ph.D Getting the Credit We Deserve: An Analysis of Residential Lending in New Castle County, Delaware: 1984-1986. Institute for Public Policy Studies, Temple University, 1989; analysis of HMDA data from 1984-1986 and 1980 U.S. Census of Population and Housing, Summary Tape File 3 data.

"...The correlations between race and the residual values are uniformly negative. After a series of market forces have been empirically controlled, the relationship between racial composition and the number or dollar volume of lending activity is negative and statistically significant. Race based market barriers to residential lending appear to be present in New Castle county..."

"In sum, the profile of lending is quite clear. Independent of lender, number of units, income level, and location, percent owner occupied percent married, and neighborhood stability, minority areas receive fewer loans than predominantly white neighborhoods."

6. Rosen, David, Ph.D. Community Credit Needs Assessment City of Oakland. Office of Community Development and Office of Economic Development and Employment, the City of Oakland, 1989. Nearly 100 direct interviews with wide-ranging representatives of borrowers, lenders, and intermediaries in both residential and commercial lending.

"...This study identifies a wide range of unmet credit needs for affordable housing, small business, minority and non-profit enterprise. Disturbingly, the study also found widespread concern about the effects of racist practices and prejudice on investment and credit availability in Oakland. The underlying causes of disinvestment in Oakland's businesses and neighborhoods are rooted in longstanding institutional practices, concerns among investors about Oakland's "image", racial prejudice,..."

7. Blossom, Teresa, Everett, David, and Gallagher, John. "The Race For Money", Detroit Free Press, 1988,: analysis of 1981-1986 HMDA and 1980 US Census data.

"Banks and savings institutions in metro Detroit make home loans in the City's White, middle-income neighborhoods at three times the rate of similar black neighborhoods, according to a Free Press study of mortgage records.

The lending gap between white and black neighborhoods in the predominantly black city increased every year from 1982 until it reached a 3-1 ratio in 1986, the most recent year records were available...."

8. Dedman, Bill. "The Color Of Money", (a four-part series on "redlining" and racially discriminatory lending patterns by banks and S&L's) Atlanta Journal-Constitution, 1988; analysis of 1981-1986 HMDA data matched with demographic data from the 1980 US Census and 1986 real estate records for 16 neighborhoods.

"Whites receive five times as many home loans as blacks from Atlanta's banks and savings and loans as blacks of the same income -and that gap has been widening each year, and Atlanta Journal-Constitution study of $6.2 billion in lending shows.

Race - not home value or household income - consistently determines the lending patterns of metro Atlanta's largest financial institutions,...

Among stable neighborhoods of the same income, white neighborhoods always received the most bank loans per 1,000 single- family homes. Integrated neighborhoods always received fewer. Black neighborhoods - including the mayor's neighborhood - always received the fewest. The study was controlled so any statistical bias would underestimate the differences between lending in black and white areas..."

9. Williams, Peter. Race and Mortgage Lending in New York City. the Center for Law and Social Justice at Medgar Evers College 1988; analysis of mortgage data for 1985 and 1986 for all HMDA-covered lenders.

Overall, predominantly white census tracts received 6 times more mortgage loans than minority tracts. Looking only at middle income tracts, those where the population was 80% or more white got 90 loans per 1,000 units of owner occupied housing, versus 40 loans per 1,000 units in middle income tracts where the population was 80% or more minority.

The report concludes that "race seems to be the sole reason for the vas differences we observed in lending patterns. Income, quality of housing stock and age did not account for the discrepancy in lending data."

10. Shlay, Anne B., Ph.D. Maintaining the Divided City: Residential Lending Patterns in the Baltimore SMSA. Institute for Policy Studies, The Johns Hopkins University, 1987; analysis of 1981-1984 HMDA data and 1980 census data.

"...Race explains why some areas received more loans than others. Accounting for normal market factors such as local income levels, residential turnover, housing values and the like, findings show that in both Baltimore and its suburbs, areas housing more blacks lost conventional single family finance compared to more white areas, net of market forces..."
"...concludes that the market area of the federally regulated depository institutions is heavily segmented by location and race....These findings suggest that part of the work of maintaining the divided city is accomplished through the residential lending practices of the federally regulated depository finance industry...."

11. Goldstein, Ira, Ph.D The Flow of Housing Capital in the Philadelphia Metropolitan Area, 1982-1984. Temple University 1986; analysis of HMDA data and 1980 census of Population and Housing data.

"...In sum, whatever means undertaken (i.e., analysis of tract means, regression analysis, or graphic depiction) there is a demonstrable spatial relationship between the racial composition of an area and mortgage activity....In other words, independent of the characteristics of the housing stock and the income of residents, black and Hispanic neighborhoods in both the city and the suburbs received less than white neighborhoods...."

12. Shlay, Anne. Credit On Color: The Impact of Segregation and Racial Transition on Housing Credit Flow in the Chicago SMSA from 1980-1983. Center for Metropolitan Planning and Research, the Johns Hopkins University, 1986; analysis of the distribution of single family mortgages made from 1980-1983 among Chicago and suburban areas using census tracts classified by the direction of racial change experienced from 1970-1980.

"...Findings show that over and above normal market mechanisms, depository institutions have continued to use racial composition and the direction of racial change as a guide for investment locations in both Chicago and the suburbs, incrementaly withdrawing credit as areas approach minority dominance..."

13. Shlay, Anne. Not In That Neighborhood: The Effects of Population and Housing On The Distribution Of Mortgage Finance Within the Chicago SMSA. Center for Metropolitan Planning and Research, the John Hopkins University, 1986; Based on lender's reports of the location of their home mortgage dispositions.

"...Findings show that credit flowed more from both depository and non-depository institutions to the suburbs or revitalizing parts of Chicago while the majority of the central city was bereft of credit. Independent of normal market factors, the racial composition of local areas explained why some areas received more lending than others and which types of loans (FHA v. Conventional). The segmentation of credit markets by race and location indicate that lenders use narrow and biased definitions of risk. Disinvestment by race and location is a normal part of the work of making residential investments in Chicago..."

14. Shlay, Anne, PH.D. Where the Money Flows: Lending patterns in the Washington, DC-Maryland SMSA. Woodstock Institute 1985; analysis of 1981 and 1982 HMDA data and housing and population data by census tract from the 1980 US Census.

"....Even more startling, income level, the most telling factor in whether a borrower can repay a loan, had no effect on the amount of lending in the District. Analysis of the characteristics of census tracts in terms of the volume and number of loans received shows that the most important characteristic influencing lending in the District was race..."

Attachment II

center for community change

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June 13, 1989

NEW RESEARCH SHOWS
S&Ls SHUN LOWER INCOME AND MINORITY NEIGHBORHOODS

New research released by the Center for Community Change raises serious questions about the way the nation's depository institutions are serving the credit needs of minority neighborhoods. Further, it calls into question the record of S&Ls, in particular, of addressing the credit needs of lower income areas.

Overview

A preliminary analysis of mortgage lending in fourteen metropolitan areas reveals that, on average, banks and savings and loans lend at a much lower rate in minority neighborhoods than in non-minority areas. This racial disparity prevails even among neighborhoods with comparable income levels. Further, the research shows that, on average, S&Ls have a smaller market share of housing loans in low and moderate income and minority neighborhoods than in middle and upper income neighborhoods, while the converse is true for commercial banks.

An analysis of the financial statements of the nation's S&Ls indicates that the percentage of assets an institution holds in housing loans declines as its reliance on cash advances from the Federal Home Loan Bank System (FHLBS) increases. Congress chartered the Federal Home Loan Banks in 1932 for the purpose of supporting the mortgage market by lending cash advances to S&Ls, which would then relend the funds as mortgage loans. However, the data shows that S&Ls are using the cash advance window for other purposes. These new findings parallel a 1988 U.S. General Accounting Office study that found that the Federal Home Loan Banks' lending operations do not support housing credit needs in any significant way, but rather serve primarily as a cash generating machine for the larger S&Ls.

The research was conducted by the Washington, DC-based Center for Community Change (CCC), a national, non-profit organization that tracks lending activities by banks and S&Ls in low and moderate income areas. The Center will be making the data and an accompanying computer program available to low

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income community groups around the country to permit these organizations to conduct their own analyses of local lending patterns.

Methodology

The data base for the mortgage lending portion of the research project was obtained from the 1986 and 1987 Federal Home Mortgage Disclosure Act (HMDA) reports. HMDA requires all banks, S&Ls, and credit unions located in metropolitan areas and with at least $10 million in assets to report each year on the geographic location of their mortgage-related lending. Fourteen metropolitan areas were selected for the study, including very large, middle size, and small cities. The selected cities were as follows: Philadelphia, Detroit, Washington, DC, Baltimore, Dallas, Oakland, Atlanta, San Antonio, Hartford, Rochester, NY, Memphis, Trenton, South Bend, and Brooklyn, NY. The data base encompassed 569,618 1-4 family mortgage loans and $2.75 billion in multi-family housing loans that were made by banks, S&Ls, and credit unions over a two year period in these fourteen metropolitan areas. The metropolitan areas chosen represent over 15% of the nation's census tracts. Thus, the data base was a large one.

In addition to an analysis of mortgage lending, the research effort analyzed the financial statements of 3,172 S&Ls. This information was obtained from FSLIC and is based on the 1987 fourth quarter Statement of Condition Reports filed by these institutions with the agency.

Specific Findings:

1. Banks and S&Ls Are More Active Mortgage Lenders in Non-Minority Areas Than In Minority Areas

Using HMDA and census data, the research project compared mortgage loan activity in non-minority census tracts with minority census tracts. The data showed that, on average, the rate of mortgage loan activity was more than three times greater in non-minority census tracts than it was in minority census tracts.

The disparities between lending activity occur even when the income level of the census tracts is taken into consideration. In middle income non-minority census tracts, depository lenders made 96.65 mortgages per 1,000 owner-occupied housing units, but they made only 34.50 mortgages per 1,000 owner-occupied housing units in middle income, minority census tracts. In moderate income, non-minority census tracts depository lenders made 83.51 mortgages per 1,000 owner-occupied housing units, but only 34.89 mortgages per 1,000 owner-occupied housing units in moderate income, minority tracts (see Data Set #1). Even in upper income census tracts the disparity prevails. Comparisons cannot be made for low income census tracts due to the high incidence of 1-4 family rental housing units.

These findings are in basic accord with earlier studies published by the Atlanta Journal-Constitution, Detroit Free-Press, and other sources which indicated the tremendous disparities in mortgage lending levels by banks and S&Ls between minority and non-minority communities.

2. On Average, S&Ls Provide a Smaller Share of Mortgage Loans in Low and Moderate Income and Minority Neighborhoods Than They Do in Middle and Upper Income Neighborhoods

S&Ls are given a number of regulatory advantages (access to the FHLBS'cash advance window and broader powers than banks) in return for serving as mortgage specialists. Yet, the research demonstrates that S&Ls are selective about where they conduct their lending. The data reveals that in comparison with commercial banks, S&Ls on average focus a higher proportion of their mortgage lending efforts in more affluent neighborhoods.

Data Set #2a & b illustrates the average S&L and commercial bank share of the 1-4 family mortgage loan market in four different neighborhood categories - low income (less than 50% of median income), moderate income (between 50-80% of median), minority (above 75% minority population) and middle/upper income (above 80% of median). The S&Ls' share of the market falls from 59.67% in middle/upper income census tracts, to 54.61% in minority tracts, to 52.13% in moderate income tracts, to 46.15% in low income census tracts. In contrast, the commercial banks' share of the market rises from 37.90% in middle/upper income neighborhoods, to 41.91% in minority neighborhoods, to 46.67% in moderate income neighborhoods, to 47.27% in low income neighborhoods. Similarly, the credit unions' share of the market rises from 1.41% in middle/upper income neighborhoods to 6.58% in lower income neighborhoods.

The declining S&L market share in less affluent and minority neighborhoods is even more dramatic for multi-family housing loans. (See Data Set #3a & b.)

3. S&Ls' Mortgage Holdings Decline As Cash Advance Use Increases

The Federal Home Loan Banks are government-sponsored enterprises, a fact that enables them to borrow funds at a preferred rate from the capital markets. These funds are re-loaned ("cash advances") to the nation's S&Ls at cheaper rates than would otherwise be available to these institutions. However, analysis of the characteristics of cash advance users indicates that these borrowings are not supporting housing needs, as the system was originally intended to do.

Data Set #4 presents information about the relationship between the mortgage holdings of S&Ls and their cash advance use. The charts show that institutions that are non-users of the Federal Home Loan Banks' borrowing window have the highest percentage of their assets in residential mortgages. The percentage of mortgage holdings declines steadily as cash advance use increases.

Conclusions

The preliminary findings point to two major conclusions:

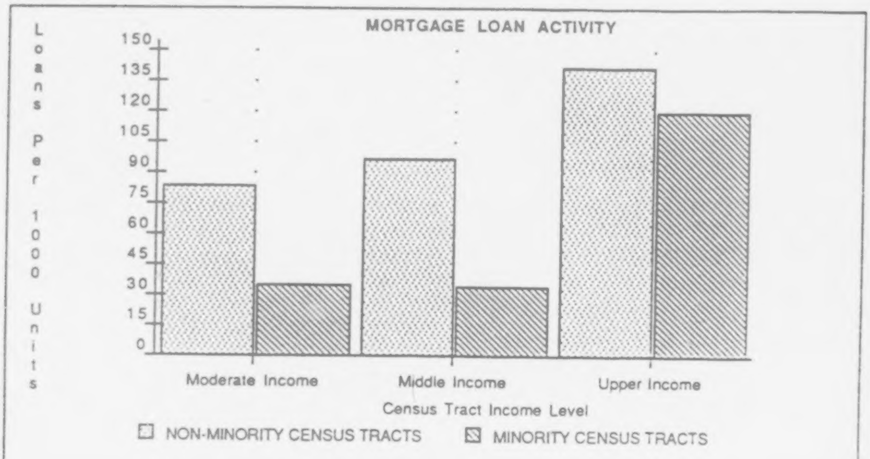
1) Expanded enforcement of the nation's civil rights and community reinvestment laws is needed to ensure that banks and S&Ls do not discriminate against minority communities.

2) More explicit requirements are needed to ensure that the Federal Home Loan Bank system promotes homeownership and mortgage lending, as it was originally intended to do.

Data Set #1

NUMBER OF 1-4 FAMILY MORTGAGES PER 1,000 OWNER OCCUPIED HOUSING UNITS

IN FOURTEEN CITIES



ALL CITIES CONSOLIDATED DATA					
All Reporters	Number of 1-4 Family Mortage Loans Per 1,000 Owner Occupied Housing Units				
	Low Income	Moderate Incom	Middle Income	Upper Income	total
Min. < 25%	678.20	83.51	96.65	141.38	111.69
Min < 10%	2650.38	66.56	96.54	140.45	111.72
10% < M < 15%	75.56	73.10	97.05	154.11	113.19
15% < M < 25%	111.91	117.96	97.05	133.60	109.99
25% < M < 50%	101.01	80.66	97.18	133.23	97.02
50% < M < 75%	70.72	66.82	93.49	100.09	81.06
Min > 75%	36.71	34.89	34.50	120.03	35.01
Subtotal	59.63	62.68	93.41	140.42	99.93

SOURCE: Home Mortgage Disclosure Act data for 1986 and 1987 for Brooklyn and the Philadelphia, Detroit, Washington (DC), Baltimore, Dallas, Oakland, Atlanta, San Antonio, Hartford, Rochester (NY), Memphis, Trenton and South Bend MSAs.

Data Set #2a

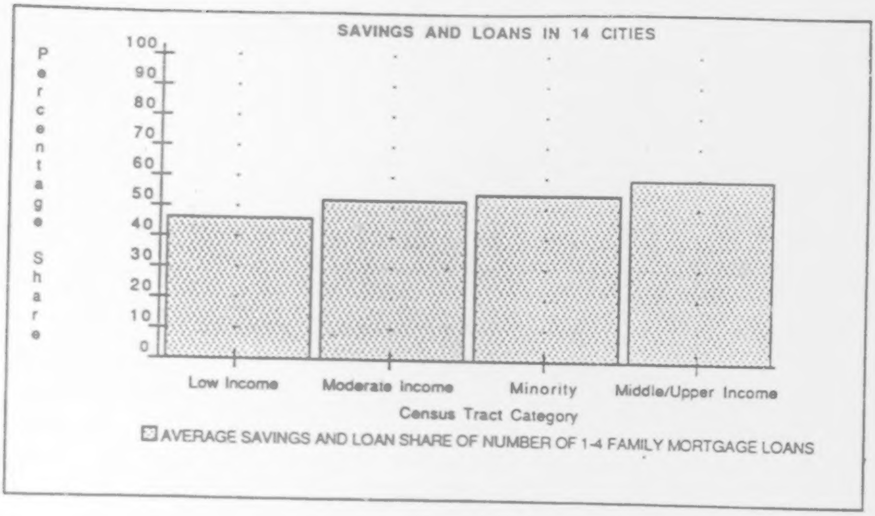
AVERAGE PERCENTAGE OF 1-4 FAMILY MORTGAGE LOANS IN 4 CENSUS TRACT CATEGORIES

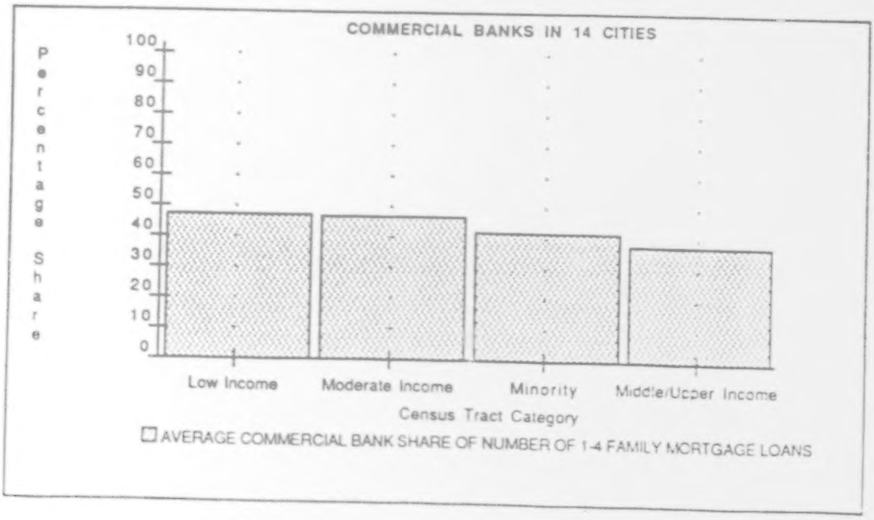
For Banks, Savings and Loans and Credit Unions in 14 Cities

ALL CITIES		Average Percentage - Number of 1-4 Family Mortgage Loans			
		Low Income	Moderate Incom	Minority	Middle/Upper In
Savings and Loans		46.15	52.13	54.61	59.67
Commercial Banks		47.27	46.67	41.91	37.90
Credit Unions		6.58	1.20	1.38	1.41
LARGER CITIES		Average Percentage - Number of 1-4 Family Mortgage Loans			
		Low Income	Moderate Incom	Minority	Middle/Upper In
Savings and Loans		53.53	59.77	63.50	69.65
Commercial Banks		41.30	38.60	34.09	28.73
Credit Unions		5.16	1.62	2.38	1.58
MEDIUM CITIES		Average Percentage - Number of 1-4 Family Mortgage Loans			
		Low Income	Moderate Incom	Minority	Middle/Upper In
Savings and Loans		49.37	51.66	60.59	56.98
Commercial Banks		40.40	47.83	38.60	41.87
Credit Unions		10.23	0.50	0.81	1.14
SMALLER CITIES		Average Percentage - Number of 1-4 Family Mortgage Loans			
		Low Income	Moderate Incom	Minority	Middle/Upper In
Savings and Loans		32.90	43.17	36.02	50.56
Commercial Banks		63.30	55.30	55.82	44.39
Credit Unions		3.80	1.53	0.82	1.54

SOURCE: Home Mortgage Disclosure Act data for 1986 and 1987 for Brooklyn and the Philadelphia, Detroit, Washington (DC), Baltimore, Dallas, Oakland, Atlanta, San Antonio, Hartford, Rochester (NY), Memphis, Trenton and South Bend MSAs.

Data Set #2b


SAVINGS AND LOANS IN 14 CITIES
Percentage Share
100
90
80
70
60
50
40
30
20
10
0
Low Income
Moderate Income
Minority
Middle/Upper Income
Census Tract Category
▨ AVERAGE SAVINGS AND LOAN SHARE OF NUMBER OF 1-4 FAMILY MORTGAGE LOANS


COMMERCIAL BANKS IN 14 CITIES
Percentage Share
100
90
80
70
60
50
40
30
20
10
0
Low Income
Moderate Income
Minority
Middle/Upper Income
Census Tract Category
▨ AVERAGE COMMERCIAL BANK SHARE OF NUMBER OF 1-4 FAMILY MORTGAGE LOANS

Data Set #3a

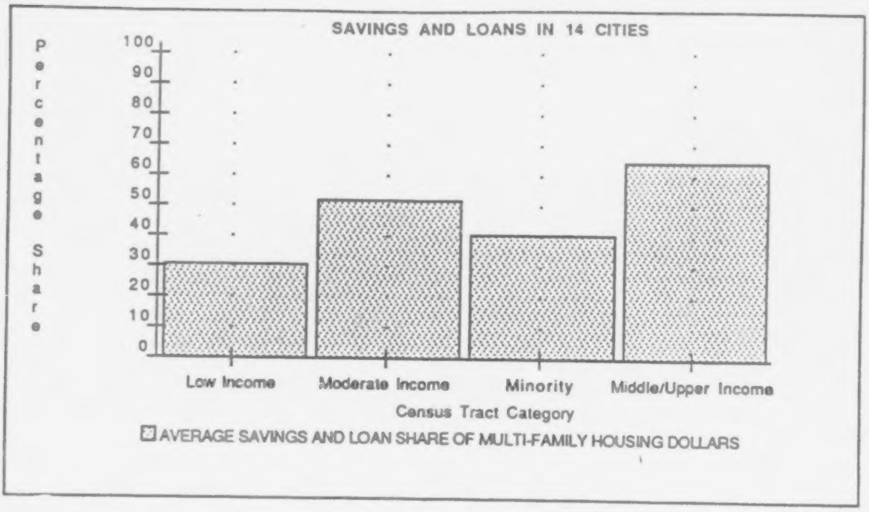
AVERAGE PERCENTAGE OF MULTI-FAMILY HOUSING DOLLARS IN 4 CENSUS TRACT CATEGORIES

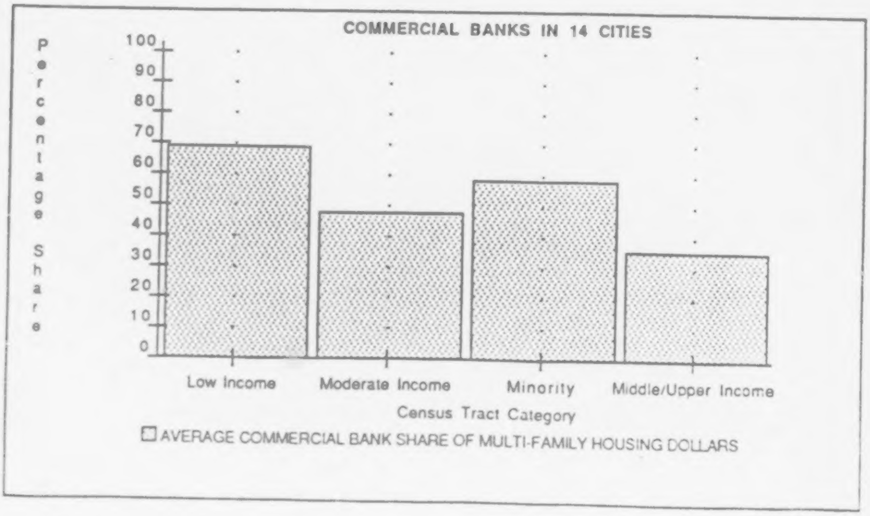
For Banks, Savings and Loans and Credit Unions in 14 Cities

ALL CITIES	Average Percentage - Multi-Family Housing Dollars			
	Low Income	Moderate Income	Minority	Middle/Upper In
Savings and Loans	30.49	51.84	40.51	64.31
Commercial Banks	69.08	47.73	58.31	35.57
Credit Unions	0.43	0.43	1.18	0.12
LARGER CITIES	Average Percentage - Multi-Family Housing Dollars			
	Low Income	Moderate Income	Minority	Middle/Upper In
Savings and Loans	37.94	57.10	41.73	78.48
Commercial Banks	61.92	42.13	55.83	21.43
Credit Unions	0.15	0.77	2.44	0.09
MEDIUM CITIES	Average Percentage - Multi-Family Housing Dollars			
	Low Income	Moderate Income	Minority	Middle/Upper In
Savings and Loans	40.08	60.57	50.59	56.48
Commercial Banks	58.96	39.09	49.02	43.29
Credit Unions	0.96	0.34	0.38	0.23
SMALLER CITIES	Average Percentage - Multi-Family Housing Dollars			
	Low Income	Moderate Income	Minority	Middle/Upper In
Savings and Loans	2.10	28.54	12.26	56.40
Commercial Banks	97.90	71.46	87.74	43.60
Credit Unions	0.00	0.00	0.00	0.00

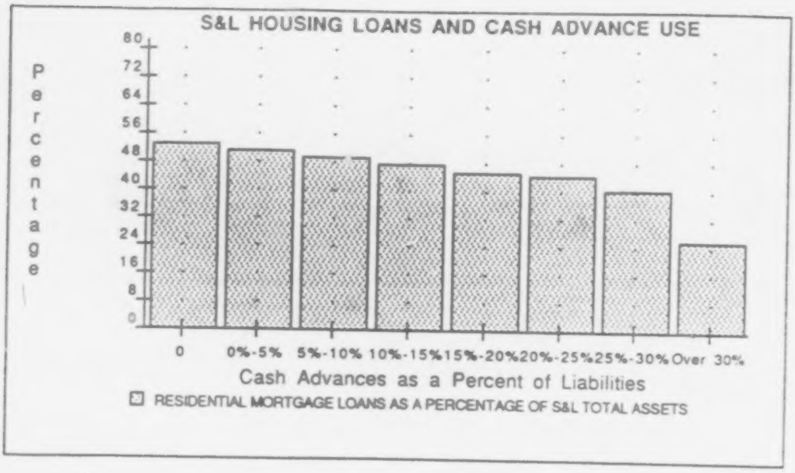
SOURCE: Home Mortgage Disclosure Act data for 1986 and 1987 for Brooklyn and the Philadelphia, Detroit, Washington (DC), Baltimore, Dallas, Oakland, Atlanta, San Antonio, Hartford, Rochester (NY), Memphis, Trenton and South Bend MSAs.

Data Set #3b


SAVINGS AND LOANS IN 14 CITIES
Percentage Share
100
90
80
70
60
50
40
30
20
10
0
Low Income
Moderate Income
Minority
Middle/Upper Income
Census Tract Category
▨ AVERAGE SAVINGS AND LOAN SHARE OF MULTI-FAMILY HOUSING DOLLARS


COMMERCIAL BANKS IN 14 CITIES
Percentage Share
100
90
80
70
60
50
40
30
20
10
0
Low Income
Moderate Income
Minority
Middle/Upper Income
Census Tract Category
▨ AVERAGE COMMERCIAL BANK SHARE OF MULTI-FAMILY HOUSING DOLLARS

Data Set #4



RESIDENTIAL MORTGAGE LOAN HOLDINGS OF SAVINGS AND LOANS AND LEVEL OF CASH ADVANCE USE								
	CASH ADVANCES AS A PERCENTAGE OF TOTAL LIABILITIES							
	0	0%-5%	5%-10%	10%-15%	15%-20%	20%-25%	25%-30%	Over 30%
NUMBER OF S&LS	1257	666	541	369	184	100	44	11
COMBINED ASSETS	136 b.	256 b.	284 b.	330 b.	168 b.	73 b.	47 b.	5 b.
($ in billions)								
1-4 FAMILY MORTGAGES	49.77	46.86	45.08	43.21	40.05	38.9	36.65	NA
MULTI-FAMILY MORTGAGES	2.91	4.06	4.32	4.47	5.23	5.63	3.62	NA
RESIDENTIAL MORTGAGES	52.68	50.91	49.41	47.68	45.28	44.54	40.27	25.66
(average percentage of total)								
(assets for S&Ls in cash advance)								
(use group)								

SOURCE: Federal Savings and Loan Insurance Corp., S&L Call Reports, December 31, 1987.

Attachment II-A

The Washington Post

REAL ESTATE

Saturday, July 15, 1989

Home Lending Study Suggests Racial Bias

Group Surveys Washington, 13 Cities

By H. Jane Lehman
Special to The Washington Post

Lenders here and in 13 cities are, on average, three times more likely to approve mortgages in areas that are predominantly white than they are in neighborhoods that are dominated by minorities, according to a new study.

The data, collected by the locally based Center for Community Change, a community activist group, "suggests at the very least that these [lending] institutions are not marketing credit as aggressively in minority neighborhoods as they do in non-minority neighborhoods," said Allen Fishbein, the organization's general counsel.

A less charitable view, Fishbein said, "suggests the possibility of discrimination, either in policies that have the effect of discriminating or in direct bias on the part of loan officers."

An official for a group representing the savings and loan industry said the study's findings are "puzzling" considering the small number of borrower discrimination complaints filed with federal regulators, but admitted that the data "raises a red flag" and indicates a need to "further examine" the situation.

A commercial banking industry spokeswoman, however, criticized the study as one "designed for PR and not for scientific analysis because the data is insufficient to prove or disprove discrimination."

The study analyzed 1986 and 1987 mortgage activity by banks, S&Ls and credit unions according to the racial makeup and income level of the census tracts covered by the 14 cities. During that period, the institutions made 569,628 single-family home mortgage loans and $2.75 billion in multifamily housing loans. To adjust for discrepancies in homeownership rates in the various neighborhoods, the study arrived at lending frequency rates by measuring how many mortgages were made for every 1,000 owner-occupied homes in an area.

In the Washington metropolitan area, the study found that the rate of mortgage lending declined as an area became predominately minority.

Lending activity plummets from a rate of 110 mortgages per 1,000 owner-occupied units when a neighborhood is less than 25 percent minority to 38 per 1,000 when minorities represent more than 75 percent of the area's population.

Nationally, a similar pattern is

See LOANS, E17, Col. 1

Suggests Racial Discrimination

LOANS, From E1

found with lending levels falling from 111 mortgages per 1,000 owner-occupied homes in largely white areas to 36 in predominantly minority census tracts.

The study's findings support other recent research reports of disparities in mortgage lending levels between minority and non-minority communities, Fishbein noted.

However, Mary-Liz Meany, chief spokeswoman for the American Banking Association, claimed the study is invalid because it does not take into account the reasons a lender may have rejected a loan, such as an insufficient down payment or an unacceptable credit history.

Socio-economic factors also can explain some of the results, Meany said. For example, low-income minorities may not trade up their homes as often as others, leading to less demand for new home loans in their areas.

"It's virtually impossible to turn this issue into a black and white issue, which is what the consumer groups have attempted to do," she said.

Fishbein acknowledged that information unavailable to the public, such as the number of applicants turned down and the reasons for their rejection, could account for some of the lower lending rates in minority communities. However, he said, "normal market factors" cannot explain the "tremendously stark differences" in lending patterns between minority and non-minority census tracts regardless of income.

Although the cities studied were not selected by random, Fishbein said the large size of the sample, which accounts for more than 15 percent of the nation's census tracts, adds legitimacy to the report's conclusions.

The study also uncovered what Fishbein calls a "surprising" finding showing that savings and loans, the traditional suppliers of mortgage credit, account for a smaller share of single-family home and multifamily mortgage lending in low-income and minority neighborhoods than do commercial banks, a reverse of the market share patterns in neighborhoods with greater affluence and fewer minorities.

In the Washington area, though, S&Ls maintain a dominant lending market share across the board for single-family loans, but fall behind the banks in multifamily lending activity.

James H. Grohl, a spokesman for the U.S. League of Savings Institutions, a trade group representing S&Ls, called that market share results a "stunner" given that 62 percent of the portfolios of solvent S&Ls are devoted to housing assets.

Fishbein hypothesized that "S&Ls are being rather selective in where they market their credit."

Pressure from community groups also could account for the larger role commercial banks are playing in poor and minority communities, Fishbein said. These groups ask federal regulators to deny an institution's merger or acquisition request if it has avoided investing in poor and minority communities. According to Fishbein, a national housing task force last year found that lenders agreed to invest $4 billion in mortgage money in these communities to mollify community groups.

> *"It's virtually impossible to turn this issue into a black and white issue."*
>
> — Mary-Liz Meany,
> American Banking Association

The ABA's Meany declined to take credit for the larger market shares the study attributed to commercial banks, again referring to the flaws her organization sees in the research.

The study also criticized S&Ls for taking advantage of subsidized cash advances from the federal home loan bank system, which carry low rates of interest, to pursue activities other than mortgage lending. The center found that the percentage of mortgage holdings declines steadily as cash advance use increases.

"The federal home loan bank system was set up to promote homeownership and mortgage lending, so this raises the question of whether reform is needed of the whole system," Fishbein said.

Grohl, however, said that the group's failure to count mortgage-backed securities in addition to mortgages held in portfolio understates the mortgage holdings of S&Ls.

Besides Washington, the study also examined lending activity in Philadelphia, Detroit, Baltimore, Dallas, Oakland, Atlanta, San Antonio, Hartford, Rochester, Memphis, Trenton, South Bend and Brooklyn.

American Banker June 16, 1989

Attachment II-B

Study Faults Home Lending Practices In Low-Income Areas of 14 US Cities

By JAY ROSENSTEIN

WASHINGTON — Mortgage lenders, especially savings and loans, are neglecting low-income and minority neighborhoods in 14 cities, a study has found.

The study, released here on the eve of a House vote to toughen community reinvestment laws, was conducted by the Center for Community Change. The Washington-based nonprofit group provides technical assistance to community groups in low-income neighborhoods.

"This study shows very clearly that disinvestment and discrimination by banks and S&Ls appear to be a problem in these communities," said Allen Fishbein, general counsel for the center.

Major conclusions of the study, which was sent to members of Congress, included the following:

- The average rate of mortgage lending by banks and thrifts, as a percentage of owner-occupied housing units, was three times higher in nonminority neighborhoods than in minority neighborhoods.
- S&Ls focus a higher proportion of their mortgage lending efforts in affluent neighborhoods than do commercial banks. The study found that the S&L share of the one-to-four-family mortgage loan market falls from about 60% in upper-income census tracts to 52% in moderate-income areas, and to 46% in low-income areas. In contrast, the bank share rises from 38% in upper-income areas to 42% in minority neighborhoods. Credit unions demonstrated a pattern of lending similar to that of banks.
- S&Ls that rely the most on low-rate cash advances from the Federal Home Loan Bank System are the institutions with the lowest percentage of assets in residential mortgages. That tendency, the study says, undermines the original intent of the cash advance program to support housing needs.

"It's our feeling that these data reinforce the need for broader public disclosure of bank lending activities," Mr. Fishbein said, such as the disclosure of agency evaluations of an institution's record under the Community Reinvestment Act. He said it also shows the need for Congress to enact affordable housing programs through the district Federal Home Loan Bank System.

In a related announcement on Thursday, Comptroller of the Currency Robert L. Clarke said his agency plans to give the public easier access to information about its decisions on applications from banks with community reinvestment problems.

The agency said that starting next month it will publish letters sent to national banks where applications have been conditionally approved or denied on grounds related to the Community Reinvestment Act. These letters were previously available only on request.

"We certainly don't condone discrimination in lending," said James Grohl, senior vice president with the U.S. League of Savings Institutions, in response to the 14-city study. "We have laws on the books, and we think those laws ought to be enforced. If there is a breakdown in enforcement, then the administration and Congress need to look at it and get it fixed."

The cities studied were Philadelphia, Detroit, Washington, Baltimore, Dallas, Oakland, Atlanta, San Antonio, Hartford, Memphis, Trenton, Brooklyn, Rochester, N.Y., and South Bend, Ind. ■

To obtain copy of report
contact:

Center for Community Change

Allen J. Fishbein
GENERAL COUNSEL
202/342-0567

1000 Wisconsin Avenue, NW, Washington, DC 20007

Attachment III

A.1

Study finds racial pattern in lending

Boston Globe 9/1/89

Inequities cited for city's blacks

By Steve Marantz
Globe Staff

Boston's black neighborhoods are suffering from a racially skewed pattern of lending by banks, thrifts and mortgage companies, and as a result are not getting a fair share of home mortgages, according to a Federal Reserve Bank of Boston study released yesterday.

Lenders are granting 24 percent fewer home loans in Boston's black neighborhoods than white neighborhoods, according to the study. The survey found that the discrepancy exists even after discounting other factors in black neighborhoods, such as lower incomes, less wealth, lower-valued housing units, and less housing development.

"This unfortunate pattern persists even after taking into account economic and nonracial characteristics that could be responsible for differences between these neighborhoods," the report concludes. "These other characteristics . . . simply do not explain the persistent pattern by race."

"While adjustments for these neighborhood characteristics reduced the size of the discrepancy in mortgage lending between white and black areas, a 24 percent difference remains," the study added.

The study found no evidence that Boston banks are engaging in redlining, an illegal practice in which banks intentionally do not loan money in minority neighborhoods.

Community leaders yesterday called the mortgage study proof of what they had long known, and bank executives said the report will serve as a catalyst for reforms. Page 32.

However, after accounting for several variables in the housing and credit markets, the analysis found that "the results . . . continue to indicate that race is an important factor" in the statistical discrepancy between the number of mortgages awarded in black and white neighborhoods.

The study did not examine the lending patterns of individual banks. But Fed president Richard Syron, describing the study's findings as "not trivial," said yesterday that he has sent a copy of the study to every bank president in New England.

Syron said he has put the region's banks on notice that the Fed will take a more aggressive regulatory stand in monitoring compliance with the Community Reinvestment Act, which requires banks to meet local credit needs.

LENDING, Page 6

■ LENDING
Continued from Page 1

While the study did not assess blame for the lending discrepancies, it said Boston banks must take steps to correct the problem.

"I do think that lending institutions have not been as aggressive as they can, should and hopefully will be in terms of understanding those neighborhoods and going out and looking for business in those neighborhoods," said Syron.

"There aren't any easy answers. I know people would like us to come up with a list and say, 'Guilty, guilty, innocent, guilty.' But it doesn't work that way. That's just the reality we have to deal with. We have to play it the way it lays."

The 36-page study, entitled "Geographic Patterns of Mortgage Lending in Boston, 1982-1987," is based on a statistical analysis of about 48,000 real estate transactions during those years in Boston's 60 neighborhoods. Unlike previous Boston lending studies, it includes data on loans made by private mortgage companies and by banks outside the metropolitan area.

Study's authors

Its co-authors are Katharine L. Bradbury, a Fed vice president; Karl E. Case, a Wellesley College professor of economics; and Constance R. Dunham, a researcher

Study finds racial pattern in lending

at the Urban Institute in Washington, D.C.

The study is a follow-up to Dunham's preliminary Fed study published in January alleging racial bias in home mortgage lending in Boston. Since then, the banking industry and community groups have taken tentative steps toward defining unmet credit needs and proposing solutions.

Elected officials, bankers and community advocates yesterday expressed concern over the Fed's findings and said that the new study should provide further impetus for finding solutions.

Mayor Flynn called on banks to take immediate action, but cautioned against pitting one neighborhood against another.

"We need to expand the overall availability of credit to meet the needs of each neighborhood, particularly for low- and moderate-income working families," said Flynn. "The Flynn administration has worked hard to develop affordable housing for Boston residents in every neighborhood. . . . I would be very upset to learn that some of Boston's lending institutions may be working at cross-purposes with this goal."

Flynn is considering legislation that would require banks to meet socially sensitive lending criteria in order to receive city deposits. Additionally, the Boston Redevelopment Authority is preparing its own study on lending practices in the city, expected to be released within the next month.

RICHARD SYRON
Findings are "not trivial"

US Rep. Joseph P. Kennedy 2d, who sponsored recent legislation to force additional disclosure of lending data, demanded an end to "bias" in lending in a strongly worded statement.

"If we are going to pump $335 billion into the savings and loan industry, we have a right to demand that credit is given to every citizen of this country, regardless of the color of their skin," said Kennedy. "If banks are going to enjoy access to the discount window of the Federal Reserve, if they are going to enjoy the benefits of federal insurance for deposits, if they are to seek help from the federal government whenever trouble hits . . . then we are going to demand an end to bias in home mortgages."

Gov. Dukakis said that he is directing administration officials to review the Fed's findings and to "use every means at our disposal to ensure that every citizen has the opportunity to own a home regardless of race or national origin."

Robert Sheridan, president of the Massachusetts Bankers Association, said that the study issues a clear challenge to the banking industry.

"People have to look to the future in identifying problems in minority neighborhoods and what can be done to respond," said Sheridan. "The challenge being issued to the banking industry is appropriate. To some degree we've met that challenge in meeting with community groups, and will continue to do so.

"Can banks do more? Absolutely. We can be more aggressive in outreach and marketing our programs. Can you build relationships? Yes."

Other factors detailed

The study detailed other factors that contribute to lending discrepancies, including the reluctance of developers and investors to do business in minority neighborhoods, and housing discrimination.

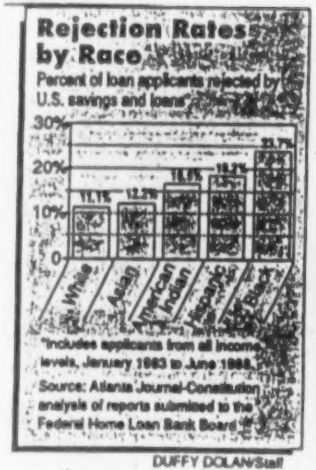
"Discrimination in the housing market, whereby blacks face barriers to moving into white neighborhoods, and reluctance by many whites to move into black neighborhoods, may reduce mobility among blacks and lead to fewer transactions and fewer mortgage loans," the study said.

"Hesitancy on the part of developers and investors to construct or rehabilitate properties in black neighborhoods would also mean fewer transactions and fewer loans."

The study also showed that banks with branches in minority neighborhoods tend not to have the lending discrepancies.

"That's the one element that gives us hope," said Dunham. "Looking at those banks with branches in the black community, we don't see that 24 percent difference. It makes us think marketing efforts can make a difference."

Attachment IV



Rejection Rates by Race

Percent of loan applicants rejected by U.S. savings and loans*

*Includes applicants from all income levels, January 1983 to June 1988.

Source: Atlanta Journal-Constitution analysis of reports submitted to the Federal Home Loan Bank Board

DUFFY DOLAN/Staff

Blacks Turned Down for Home Loans From S&Ls Twice as Often as Whites

By Bill Dedman

Staff Writer

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Blacks are rejected more than twice as often as whites when they apply for home loans at America's savings and loans, according to government records of $1 trillion in loan applications analyzed by The Atlanta Journal-Constitution.

The records of 10 million applications from every savings and loan in the country reveal a lending gap so pervasive and so wide that in much of the country high-income blacks are rejected at the same rate as low-income whites.

The loan records suggest that redlining — refusing to lend in an area because of race — has persisted and may have grown worse in the 1980s as federal regulators decreased enforcement of fair-lending laws.

In integrated neighborhoods, the rejection patterns appear to penalize both white and black homebuyers. Homebuyers of any race in upper-income areas that are at least 25 percent minority were rejected at the same rate as homebuyers in poor white neighborhoods.

The rejection rates were derived from a national analysis of loan applications by race, sex and marital status. The Journal-Constitution sorted computerized summaries of 10 million loan applications submitted from 1983 to mid-1988 at the nation's 3,100 savings and loan associations and mutual savings banks. Those institutions

LOANS Continued on 10A

Loans

From Page 1A

make 50 percent of America's home loans.

The raw statistics were obtained through a Freedom of Information Act request to the Federal Home Loan Bank Board, which regulates savings and loans. In settling a civil rights suit 10 years ago, the board agreed to collect and analyze the numbers. Each year since, it has diligently collected the numbers and stored them in a computer. But it has never analyzed them.

Loan statistics do not by themselves prove discrimination, since they reveal nothing about the debt burdens or credit histories of applicants.

But Home Loan Bank Board regulations say statistical disparities should be examined for clues to illegal discrimination.

"On the face of it, it looks like what you have there is a great big red flag," said Jerauld C. Kluckman, director of compliance programs for the Bank Board.

For example, the records show that blacks, besides being rejected more than twice as often as whites, withdraw applications 21 percent more often and receive no decision on loan applications 23 percent more often.

Counting these other factors, 50 percent of blacks who fill out loan applications receive loans, compared with 65 percent of whites.

"I can't argue with the numbers. Clearly we've got a problem, and the powers that be have got to agree on a way to deal with it," said Richard Tucker, director of the Bank Board's Office of Community Investment. "It's been a bad time. The question is now what are we going to do with this data while we struggle with our other responsibilities for safety and soundness."

Among other results of the study:

- The nationwide rejection rate for loan applicants of all incomes was 11.1 percent for whites, 12.2 percent for Asians, 16.5 percent for American Indians, 18.2 percent for Hispanics, and 23.7 percent for blacks.
- The black-white disparity in rejection rates was widest in the Plains (30.9 percent black vs. 12.6 percent white) and the Midwest (29.6 percent vs. 12.2 percent), even though blacks in the two regions have the nation's highest incomes relative to whites. The gap was slightly narrower in the South (24.1 percent vs. 10.2 percent), where blacks have the lowest incomes relative to whites. The disparity was less in the West (25.1 percent vs. 14.4 percent) and the Northeast (13.4 percent vs. 9.1 percent).
- Throughout the country, high-income blacks were rejected more often than low-income whites in 85 of the 100 largest metro areas in at least one of the past five years. In 35 of the 100 areas, high-income blacks were rejected more often than low-income whites in at least three of the five years.
- The disparities appear to have increased substantially when compared with a more limited federal study of 17 cities in 1974 using data from both banks and savings and loans. The black-white gap has roughly doubled in 13 of the 17 cities: Atlanta, Baltimore, Bridgeport, Conn.; Buffalo, N.Y.; Chicago; Cleveland; Galveston-Texas City, Texas; Jackson, Miss.; Jersey City, N.J.; Memphis, Tenn.; Tampa-St. Petersburg, Fla.; Topeka, Kan.; and Washington. The gap narrowed in Montgomery, Ala.; San Antonio, Texas; San Diego, Calif.; and Tucson, Ariz.
- Race is a much better predictor of a loan application's success than sex or marital status, although male and married applicants do fare somewhat better than others. Applications submitted by women were rejected 13 percent more often than applications with at least one male applicant. Unmarried applicants were rejected 22 percent more often than marrieds, and separated applicants were rejected 31 percent more often than marrieds.

The rankings of cities do not appear to be controlled by city size, minority population, or the gap between black and white incomes.

'Don't Have a Good Answer'

Industry officials said they were surprised by the racial disparities.

"Perhaps we need to have our research department do a little research on that and see if we can't come up with some reasons," said Barney R. Beeksma of Oak Harbor, Wash., chairman of the U.S. League of Savings Institutions, an industry trade association. "When you look at 23.7 percent rejected for blacks and 11.1 percent for whites, you're dealing with a number twice as large. That's troubling.

"As for people being discriminated against because they're black or minority, I've never heard of that. They must be getting a higher percentage of unqualified applicants. Or many of those applications from blacks may be coming out of very depressed neighborhoods.

"On the other hand, most people who can't qualify don't even apply or they're weeded out by a Realtor because they don't have the income. You're dealing here with people who think they can get a loan, who are willing to pay an application fee. I admit I probably don't have a good answer for that."

Credit discrimination has gained more public attention in the past year with the release of several studies of lending patterns.

A Journal-Constitution study published last May showed that banks and savings and loans in metro Atlanta made five times as many loans per 1,000 households in middle-income white areas as in black areas of the same income.

This month a draft of a study by the Federal Reserve Bank of Boston was published, suggesting that lenders in that city have a "racial bias."

Because each of those studies was based on loans made, with only estimates of loan demand, this new nationwide study adds a missing piece to the redlining puzzle: actual application data.

Redlining and other forms of credit discrimination have several adverse effects.

Without equal access to credit, community leaders say they watch their neighborhoods slide. When people cannot borrow money to buy or fix up houses, property values stagnate or decline.

Credit discrimination also perpetuates differences in income and wealth between the races from generation to generation. Homeownership is the main way that American families accumulate and hold wealth. Americans borrow against their homes for education, for vacations, for emergencies, for retirement. For most parents, a home is the most valuable part of the estate they will leave to their children.

Weakened Regulatory System

Civil rights activists point to several indicators that the Reagan administration has weakened the regulatory system built up in the 1960s and '70s to stop redlining.

Bank regulators reduced the number of examiner hours devoted to consumer regulations, including fair-lending laws, by 74 percent from 1981 to 1984; the Justice Department's Civil Rights Division has reduced the number of attorneys and staff dealing with credit cases; the Department of Housing and Urban Development quit collecting data on the location of FHA loans.

Although the bank regulatory agencies have reported declines in lender compliance with technical aspects of the Equal Credit Opportunity Act, they have not referred a case of credit discrimination to the Justice Department for prosecution since 1978.

In the 1980s, regulators have had something of an alibi, the ongoing crisis regarding the safety and soundness of banking institutions, particularly savings and loans.

> 'I can't argue with the numbers. Clearly we've got a problem, and the powers that be have got to agree on a way to deal with it. . . . The question is now what are we going to do with this data while we struggle with our other responsibilities for safety and soundness.'
>
> **— Richard Tucker**
> **Bank Board official**

"I regret to report that, as a result of this situation, we did not allocate sufficient resources to the enforcement of . . . consumer-related issues," M. Danny Wall, chairman of the Bank Board, testified in March to the Senate Banking, Housing and Urban Affairs Committee. "The Bank Board has recently increased its activity in the area . . . after a long lull. There is still much work to be done."

Last year Congress considered measures to strengthen the Community Reinvestment Act, known as the anti-redlining law because it places upon financial institutions an "affirmative obligation" to serve the credit needs of all segments of their communities. The House Banking, Finance and Urban Affairs Committee approved the bill, but in the Senate it was tied to a measure expanding the power of banks to issue securities; that measure languished.

Congressional advocates for neighborhood reinvestment say the findings on loan rejection rates increase the pressure for reform.

"We will call on the Justice Department as well as the Federal Home Loan Bank Board to pursue these results with the full force of the law," said Rep. Joseph P. Kennedy II, the Boston Democrat and a member of the House Banking Committee. "And we will ask the other bank regulators to collect and analyze similar information as well."

Two Data Systems Shut Down

Two bank regulatory agencies, other than the Bank Board, did collect such data from 1978 to 1981, but gave it up when the court order requiring it expired.

The entire bank regulatory system was sued in 1976 by 10 civil rights and housing groups, who accused the regulators of willful failure to enforce the 1968 Fair Housing Act and the 1974 Equal Credit Opportunity Act.

To settle the suits, three of the agencies signed agreements to improve enforcement, including collection of data on the race, sex and marital status of applicants. The court orders said the government agreed to collect data, "not only to settle the lawsuit, but also to further its existing commitment to effective enforcement of its non-discrimination policies."

Two of the agreements expired after three years. As soon as their settlements ended, the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corp. shut down their data system. The bank agencies argued that data didn't prove anything, and collecting it placed an unnecessary and costly burden on financial institutions.

The settlement with the Federal Home Loan Bank Board included no time limit. It agreed, in perpetuity, to "develop and implement a system for the collation and analysis" of the lending data. It developed the system and it stores the information in a computer, but it doesn't analyze it.

Instead of studying national totals, all the regulatory agencies say they study application logs at individual lending institutions during compliance examinations. Those can be spotty, however. The Office of the Comptroller examines only 35 to 50 banks a year on fair-lending issues — out of 4,500, meaning a bank could go 128 years without such an exam.

"This is not something we feel very good about," said Leonora S. Cross, the office's director of communications.

Any fair-lending enforcement at all will look like a big change up in Oak Harbor, Wash., home of Mr. Beeksma, chairman of the savings and loan league and a lender with 30 years in the business.

"To my knowledge, the Equal Credit Opportunity Act statistics have never been anything more than a collection of data," Mr. Beeksma said. "I've never heard of an examiner coming in and saying, 'You're rejecting more blacks than whites. You're doing this wrong.' "

Loan Rejection Rates by Race in 50 Largest U.S. Cities

Metro areas ranked by ratio of black to white rejection rates

Metro area	Black rejection rate	White rejection rate	Black/White rejection ratio
1. Milwaukee, Wis.	24.2%	6.2%	3.90:1
2. Pittsburgh, Pa.	31.2%	8.2%	3.80:1
3. Cleveland, Ohio	31.4%	8.4%	3.74:1
4. Chicago, Ill.	27.6%	7.6%	3.63:1
5. Detroit, Mich.	32.5%	9.1%	3.57:1
6. Norfolk-Virginia Beach-Newport News, Va.	26.5%	7.7%	3.44:1
7. Charlotte-Gastonia, N.C.-Rock Hill, S.C.	26.1%	8.0%	3.26:1
8. Indianapolis, Ind.	27.9%	8.7%	3.21:1
9. Baltimore, Md.	24.2%	7.6%	3.18:1
0. Memphis, Tenn.-Ark.-Miss.	22.2%	7.3%	3.04:1
1. Kansas City, Mo.	34.5%	11.4%	3.03:1
2. St. Louis, Mo.-Ill.	36.8%	12.3%	2.99:1
3. Dayton-Springfield, Ohio	29.2%	10.0%	2.92:1
4. Boston, Mass.	26.5%	9.1%	2.91:1
5. Rochester, N.Y.	27.8%	9.9%	2.81:1
5. Minneapolis-St. Paul, Minn.-Wis.	19.6%	7.2%	2.72:1
7. Louisville, Ky.-Ind.	34.5%	12.7%	2.72:1
3. Cincinnati, Ohio-Ky.-Ind.	27.3%	10.1%	2.70:1
New York, N.Y.	20.0%	7.6%	2.63:1
Columbus, Ohio	22.9%	9.3%	2.46:1
Birmingham, Ala.	27.1%	11.1%	2.44:1
Philadelphia, Pa.-N.J.	17.5%	7.3%	2.40:1
Tampa-St. Petersburg-Clearwater, Fla.	34.3%	14.6%	2.35:1
Fort Worth-Arlington, Texas	20.4%	9.1%	2.24:1
Phoenix, Ariz.	32.1%	14.4%	2.23:1
Atlanta	**23.3%**	**10.6%**	**2.20:1**

Metro area	Black rejection rate	White rejection rate	Black/White rejection ratio
27. San Antonio, Texas	23.5%	10.7%	2.20:1
National average	**23.7%**	**11.1%**	**2.14:1**
28. Houston, Texas	30.2%	14.1%	2.14:1
29. Denver, Colo.	34.5%	16.3%	2.12:1
30. Newark, N.J.	13.1%	6.2%	2.11:1
31. Dallas, Texas	26.6%	12.7%	2.09:1
32. New Orleans, La.	35.4%	17.4%	2.03:1
33. Seattle, Wash.	19.2%	9.6%	2.00:1
34. Buffalo, N.Y.	22.6%	11.6%	1.95:1
35. Sacramento, Calif.	27.9%	15.1%	1.85:1
36. Washington, D.C.-Md.-Va.	15.7%	8.5%	1.85:1
37. Fort Lauderdale-Hollywood-Pompano Beach, Fla.	27.5%	15.0%	1.83:1
38. Los Angeles-Long Beach, Calif.	23.2%	12.7%	1.83:1
39. San Francisco, Calif.	18.1%	10.2%	1.77:1
40. San Jose, Calif.	21.6%	12.4%	1.74:1
41. Bergen-Passaic, N.J.	11.0%	6.4%	1.72:1
42. San Diego, Calif.	36.0%	21.0%	1.71:1
43. Oakland, Calif.	23.2%	13.6%	1.71:1
44. Salt Lake City-Ogden, Utah	16.3%	9.7%	1.68:1
45. Miami-Hialeah, Fla.	28.6%	17.3%	1.65:1
46. Riverside-San Bernardino, Calif.	27.4%	16.7%	1.64:1
47. Nassau-Suffolk, N.Y.	14.5%	9.0%	1.61:1
48. Middlesex-Somerset-Hunterdon, N.J.	21.9%	14.9%	1.47:1
49. Anaheim-Santa Ana, Calif.	23.3%	16.7%	1.40:1
50. Portland, Ore.	17.5%	15.2%	1.15:1

reas ranked are Metropolitan Statistical Areas for January 1985 through June 1988 Source: Reports filed with Federal Home Loan Bank Board

Loan Rejection Rates by Race in 50 Largest Southern Cities

Metro areas ranked by ratio of black to white rejection rates

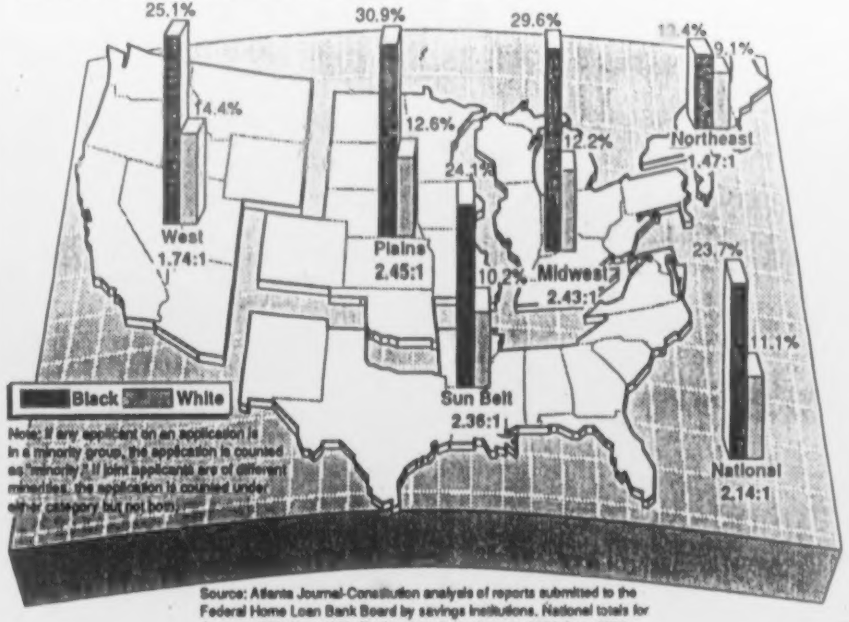
Metro area	Black rejection rate	White rejection rate	Black/White rejection ratio
1. Roanoke, Va.	25.2%	6.0%	4.20:1
2. Melbourne-Titusville-Palm Bay, Fla.	27.7%	6.9%	4.01:1
3. Savannah, Ga.	**38.5%**	**9.6%**	**4.01:1**
4. Lynchburg, Va.	29.4%	7.5%	3.92:1
5. Clarksville, Tenn.-Hopkinsville, Ky.	21.5%	5.6%	3.84:1
6. Augusta, Ga.-S.C.	**17.5%**	**4.7%**	**3.72:1**
7. Raleigh-Durham, N.C.	14.4%	3.9%	3.69:1
8. Albany, Ga.	**39.9%**	**10.9%**	**3.66:1**
9. Shreveport, La.	21.3%	6.0%	3.55:1
10. Columbus, Ga.-Ala.	**31.2%**	**8.8%**	**3.55:1**
1. Norfolk-Virginia Beach-Newport News, Va.	26.5%	7.7%	3.44:1
12. Macon-Warner Robins, Ga.	**21.2%**	**6.2%**	**3.42:1**
3. Huntsville, Ala.	25.3%	7.4%	3.42:1
4. Tallahassee, Fla.	18.0%	5.3%	3.40:1
5. Greensboro-Winston-Salem-High Point, N.C.	16.1%	4.9%	3.29:1
6. Charlotte, Gastonia, N.C.-Rock Hill, S.C.	26.1%	8.0%	3.26:1
7. Biloxi-Gulfport, Miss.	26.8%	8.3%	3.23:1
8. Memphis, Tenn.-Ark.-Miss.	22.2%	7.3%	3.04:1
9. Greenville-Spartanburg, S.C.	26.9%	8.9%	3.02:1
0. Knoxville, Tenn.	14.5%	4.9%	2.96:1
1. Little Rock-North Little Rock, Ark.	32.7%	11.1%	2.95:1
2. Lakeland-Winter Haven, Fla.	26.4%	9.1%	2.90:1
3. Louisville, Ky.-Ind.	34.5%	12.7%	2.72:1
4. Charleston, S.C.	24.2%	9.2%	2.63:1
5. Jacksonville, Fla.	33.5%	12.8%	2.62:1
6. Nashville, Tenn.	23.1%	9.2%	2.51:1
27. Baton Rouge, La.	29.5%	11.9%	2.48:1
28. Birmingham, Ala.	27.1%	11.1%	2.44:1
29. Chattanooga, Tenn.-Ga.	16.9%	7.0%	2.41:1
30. Austin, Texas	28.1%	11.7%	2.40:1
31. Tampa-St. Petersburg-Clearwater, Fla.	34.3%	14.6%	2.35:1
32. Jackson, Miss.	24.8%	10.7%	2.32:1
33. Montgomery, Ala.	34.0%	14.7%	2.31:1
34. Fort Worth-Arlington, Texas	20.4%	9.1%	2.24:1
35. Johnson City-Kingsport-Bristol, Tenn.-Va.	19.3%	8.7%	2.22:1
36. West Palm Beach-Boca Raton-Delray Beach, Fla.	29.5%	13.3%	2.22:1
37. Atlanta	**23.3%**	**10.6%**	**2.20:1**
38. San Antonio, Texas	23.5%	10.7%	2.20:1
39. Midland, Texas	19.2%	8.8%	2.18:1
National average	**23.7%**	**11.1%**	**2.14:1**
40. Houston, Texas	30.2%	14.1%	2.14:1
41. Mobile, Ala.	32.7%	15.3%	2.14:1
42. Dallas, Texas	26.6%	12.7%	2.09:1
43. Lexington-Fayette, Ky.	20.5%	9.8%	2.09:1
44. New Orleans, La.	35.4%	17.4%	2.03:1
45. El Paso, Texas	31.1%	16.2%	1.92:1
46. Washington, D.C.-Md.-Va.	15.7%	8.5%	1.85:1
47. Fort Lauderdale-Hollywood-Pompano Beach, Fla.	27.5%	15.0%	1.83:1
48. Orlando, Fla.	25.9%	14.8%	1.75:1
49. Miami-Hialeah, Fla.	28.6%	17.3%	1.65:1
50. Lafayette, La.	22.3%	15.3%	1.46:1

Areas ranked are Metropolitan Statistical Areas for January 1985 through June 1988

Source: Reports filed with Federal Home Loan Bank Board

Comparing Loan Rejection Rates by Race

Percentage of black and white applicants rejected by savings institutions and ratio of black to white rejections in regions of the United States.



Note: If any applicant on an application is in a minority group, the application is counted as "minority." If joint applicants are of different minorities, the application is counted under either category but not both.

Source: Atlanta Journal-Constitution analysis of reports submitted to the Federal Home Loan Bank Board by savings institutions. National totals for January 1983-June 1988. Regional totals for January 1985-June 1988.

DUFFY JAMES DOLAN/Staff

Senator **Dixon**. Well, thank you. That's very useful and that suggestion will be taken under consideration, I assure you.

Mr. Wade Henderson and Mr. Stephen M. Dane, representing the Leadership Conference on Civil Rights, we are pleased to have you here.

Who wants to proceed to divide this seven minutes? Mr. Henderson.

WADE HENDERSON AND STEPHEN M. DANE, REPRESENTING THE LEADERSHIP CONFERENCE ON CIVIL RIGHTS, WASHINGTON, DC

Mr. **Henderson**. Thank you, Mr. Chairman.

I am Wade Henderson, and my colleague, Stephen Dane, and I greatly appreciate the opportunity to present the views of the Leadership Conference on Civil Rights on the issue of mortgage discrimination.

The Leadership Conference on Civil Rights is a coalition of 185 national organizations committed to the full and effective enforcement of our Civil Rights laws.

The Conference has had a long-standing interest in providing Fair Housing opportunities for our Nation's citizens and in the issue of mortgage discrimination.

Now, the Conference was actively involved, for example, in the passage and lobbied strongly in support of the recent enacted Fair Housing Amendments Act of last year, and we also vigorously supported the reporting requirements in the S&L, which are the subject of today's discussion.

Mr. Chairman, we commend you, Senator Riegle and your colleagues for your longstanding commitment to this issue, your leadership in this area and your persistence in attempting to root out evidence of the discrimination which we as a Conference Coalition believe clearly exist.

As a preliminary matter, we wish to acknowledge as well the commitment of Secretary Kemp and his representatives for the kind of vigorous enforcement of these issues, the effective enforcement of our Nation's laws in this area, that we believe the Secretary of Housing should undertake. And we are pleased that this commitment was made today for the record.

We juxtapose that commitment, however, in great disbelief with the comments that were made by the representatives of the regulatory agencies here today. We associate ourselves with your comments that, indeed, in the face of the kind of evidence which we believe clearly exists, which we have documented as part of our testimony, that to assert that there is doubt about the existence of discrimination in this area we believe strange credibility.

My colleague, Mr. Dane, will present our recommendations and we together will stand ready for questions at the conclusion.

Senator **Dixon**. Thank you, Mr. Henderson.

Mr. Dane.

Mr. **Dane**. Thank you, Mr. Henderson. Thank you, Senator Dixon. I am pleased to be here today to relate a few small specific examples of my experience with mortgage lenders as a private attorney involved in extensive litigation.

The only disappointment I have is that the regulators and their key staff have left when we came up to testify. I was going to invite some of them to come work with me for a year or so for, in the course of my litigation experience, I have been able to observe, albeit after the fact, what the banking agencies are generally not sure exists and which they cannot seem to find during their examination process.

The discrimination in mortgage lending with which I've become familiar is not necessarily malicious or abusive. Indeed, in many cases, it's often unconscious. It, nevertheless, has been found to exist and is generally embodied in some sort of unfounded reluctance to engage in mortgage lending in certain neighborhoods.

I want to distinguish that from discrimination on the basis of the applicants themselves, which I've had very little experience or exposure to, or having found.

I cite one specific example, the National Bank, who discouraged my client from even submitting an application because, and I quote:

"We don't do business in that part of town."

When pressed further by my client to explain that, the loan officer indicated that their bank was relatively small and did not have the staff to police the area. The area involved in that case was the minority and low-income part of the city. I have not yet determined what sort of police staff the lender needed or used in the white neighborhoods.

I also call your attention to the Federal Savings and Loan, who justified its dismal lending record in the central city by stating, and here's another quote, that:

"Most people would not find it to be a desirable place to live." I close that quote.

I once deposed a bank underwriter who, after admitting that the applicants were qualified for the loan and that the appraised value of the property far exceeded the loan request, nevertheless, refused to approve the loan because there were some vacant homes in the area.

Again, the area involved was a 90 percent minority neighborhood in the central city.

I call your attention to the private mortgage insurer who refuses to insure properties less than $30,000. In some cities, virtually eliminating from the conventional mortgage market 70-80 percent of the minority housing stock.

I call to your attention the federally chartered savings and loan who rejected an application for a 90/10 mortgage loan from an integrated neighborhood based upon a rationale that was (a) not included in its written underwriting guidelines; (b) it initially said was in Fannie Mae's guidelines, but in fact was not; and (c) was apparently not important enough to reject the six other similar loans that we discovered in discovery from the white neighborhoods, all of which were approved.

I call your attention to the savings and loan that we discovered had old and outdated underwriting guidelines that, if applied in every case, and the underwriting guidelines are never applied in every case, would have prohibited maximum financing for any property over 30 years old, which would have wiped out virtually all of the central city in that particular area.

And, finally, the appraiser who, when defining the relevant neighborhood for the dwelling that was the subject of her appraisal, excluded from her definition of the neighborhood "the beautiful new homes only two blocks away," because in her opinion, they were too nice for this neighborhood. Her neighborhood, again, was a 90 percent minority central city neighborhood.

These are but a few examples of how unfounded assumptions about the safety or desirability of central city minority neighborhoods continue to influence mortgage lenders and the related mortgage lending service industry, such as the private mortgage insurance industry and the appraisal industry.

We agree with almost all of the regulators that such discrimination is difficult to detect and may not in all cases be intentional but it is there, and it is impeding the flow of conventional mortgage funds to minority and integrated neighborhoods. It's an inequity that exists throughout this country that we hope this Committee will pursue and, hope, will attempt to eliminate.

[The complete prepared statements of Wade Henderson and Stephen Dane follow:]

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STATEMENT

OF THE

LEADERSHIP CONFERENCE ON CIVIL RIGHTS

ON

MORTGAGE DISCRIMINATION

BEFORE

SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

UNITED STATES SENATE

October 24, 1989

"Equality In a Free, Plural, Democratic Society"

Statement of the Leadership Conference on Civil Rights Concerning Mortgage Discrimination

Stephen M. Dane, Esq. and Wade J. Henderson, Esq.[1]

Mr. Chairman and Members of the Subcommittee:

We appreciate the opportunity to present the views of the Leadership Conference on Civil Rights on the issue of mortgage discrimination and on reports of loan discrimination submitted by the federal financial institution regulatory agencies and the Department of Housing and Development pursuant to Section 1220 of the Financial Institutions Reform, Recovery, and Enforcement Act.

The Leadership Conference on Civil Rights (LCCR), a coalition of 185 national organizations representing minorities, women, disabled persons, senior citizens, labor, religious groups and minority businesses and professions has had a long-standing interest in the issue of mortgage discrimination and financial "redlining" practices. The LCCR has previously endorsed legislation which would make it unlawful for a lending institution to refuse mortgage or home improvement loans on all or substantially all property in a particular geographic area because of the racial or ethnic composition of the neighborhood.

1.Stephen M. Dane, Esq. is a partner with law firm of Cooper, Straub, Walinski and Cramer. Wade J. Henderson is Associate Director of the Washington National Office of the American Civil Liberties Union.

Indeed, the LCCR vigorously supported the "Kennedy/Gonzalez" amendment to the recently enacted "S&L bail-out" bill which strengthened the disclosure provisions of the Community Reinvestment Act (CRA) and the Home Mortgage Disclosure Act (HMDA). As this Committee knows especially well, Both CRA and HMDA were enacted in response to the documented concern about redlining practices and their contribution to racial discrimination. However, the public disclosure provisions of CRA and HMDA have proven over time to be inadequate in providing the data needed to more accurately determine whether a lending institution's practices are discriminatory.

I. MORTGAGE LENDING DISCRIMINATION CONTINUES TO BE A PROBLEM IN THIS COUNTRY

Evidence that minority applications and minority neighborhoods continue to suffer from mortgage lending discrimination was recently summarized by the Citizens' Commission on Civil Rights in its 1989 report, One Nation, Indivisible: The Civil Rights Challenge for the 1990s. This report noted that even the "most recent access-to-credit studies conclude that race still plays the most significant role in determining who gets conventional mortgage financing."2/ Although

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2. Report of the Citizens' Commission on Civil Rights, One Nation, Indivisible: The Civil Rights Challenge for the 1990s 250 (1989).

it has not conducted any large scale studies of the problem,3/ even the federal government has noted continuing equal credit problems.4/

Last year in a four-part, Pulitzer Prize winning series entitled "the Color of Money", the Atlanta Journal/Constitution dramatically documented how home mortgage lending practices in the Atlanta area discriminated against African Americans. Recent reports from other cities including New York, Detroit, Boston and Washington, DC have heightened our concern over the magnitude of the problem.

Section 1220 of the Financial Institutions Reform, Recovery, and Enforcement Act requires the financial regulatory agencies and HUD to submit reports to Congress containing findings on the

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3. The federal financial regulatory agencies acknowledge that they lack sufficient data to determine whether mortgage lending discrimination persists. The FDIC concedes that it maintains no aggregate mortgage lending data reflecting acceptance and rejection rates. Federal Deposit Insurance Corporation, Report on Loan Discrimination Pursuant to Section 1220, Oct. 12, 1989, B5, p.1. Even the information it requires its member banks to collect on log sheets is unavailable to it in a centralized location or in an aggregate format. *Id*. at 3. The Comptroller of the Currency admits having no relevant statistics, and the data it does collect is not readily retrievable. Comptroller of the Currency, Report on Loan Discrimination Pursuant to Section 1220, Oct. 12, 1989, at p.1.

The Office of Thrift Supervision points out that its data collection system (which is the most comprehensive of all the financial regulators) does not enable conclusions to be drawn regarding the existence of discrimination. Office of Thrift Supervision, Report on Loan Discrimination Pursuant to Section 1220, Oct. 9, 1989, at 2. The Federal Reserve Board "does not currently have mortgage loan acceptance or rejection statistics of the type contemplated by Section 1220."

4. Citizens' Commission Report, supra, at 251.

extent of discriminatory lending practices by mortgage lenders. Although we have had only a very short time within which to review these reports (except the report to be submitted by HUD, which we have not seen at all), we offer the following preliminary comments.

We first note that none of the financial regulatory agencies takes a clear position on whether there exists in this country a mortgage lending discrimination problem. They contend either that they lack sufficient data from which a definitive answer can be given, or that their examinations have not revealed any noticeable problems. The Federal Reserve Board, for example, explains in great detail how its consumer compliance examinations are conducted, but never says how many of those examinations in the past decade have resulted in a finding that discrimination had occurred. It only says that it "seldom" makes such a finding. Federal Reserve Board Report at pp. 9-16. Except for the Federal Reserve Board, none of the reports review or mention the many disturbing HMDA studies that have been performed in recent years.

At least two of the agencies, however, acknowledge that present known lending patterns raise troubling questions. The Office of Thrift Supervision states that a review of the data within its possession indicate nationwide differences in acceptance and rejection rates based on both race of the applicant and census tract characteristics. OTS Report at 1-2. The Board of Governors of the Federal Reserve System points out "the presence of differential lending patterns across neighborhoods ...". Federal Reserve Board Report at 19. Although these agencies draw no definitive conclusions, their reports justify vigorous congressional oversight in this area. Mr. Chairman and Members of Committee, the Leadership Conference commends you for taking a major step in this direction today.

A recent increase in litigation involving mortgage lending discrimination claims is further evidence that discriminatory activity by lenders may be on the rise rather than in decline. Over a dozen mortgage lending discrimination cases have been filed in two midwestern cities (Gary, Indiana and Toledo, Ohio) alone. This recent litigation has involved loan originators, secondary market buyers, appraisers, and private mortgage insurers. Fair housing advocates have in the past few years acknowledged increasing problems in the mortgage lending discrimination field.

This is an unfortunate state of affairs, particularly in light of the fact that there now exist at least nine federal statutes and almost a dozen different regulations that relate in some way to discrimination in housing finance. Many of these laws were designed to be enforced primarily by the federal government, especially the federal financial regulatory agencies. Unfortunately, those agencies have been more concerned in the recent past with safety and soundness issues, and have generally ignored the area of civil rights.

II. WHO IS ENFORCING THE LAWS PROHIBITING DISCRIMINATION IN HOUSING FINANCE

A. Not HUD or the Financial Regulatory Agencies

In 1977 this Committee harshly criticized the federal financial regulatory agencies for their failure to enforce the nation's anti-discrimination laws.[5] In March, 1988 this Committee again heard testimony regarding those agencies' enforcement efforts with respect to the Community Reinvestment Act.[6] At those hearings fair housing advocates and researchers were united in their criticism of the financial regulatory agencies. Statistics submitted by the agencies and their critics demonstrated that the CRA rating system used by the agencies is misleading, ineffective, and arbitrary. The agencies' examination procedures were shown to be ineffective because CRA and fair lending issues are not deemed to be important, examiners are not adequately trained in CRA and fair lending matters, too few resources are allocated to the CRA portions of examinations, and the examinations are conducted too infrequently. There was agreement that the agencies' application review and CRA protest procedures are weak, inherently deficient, and often inconsistently followed.[7]

The FDIC in its report takes the position that its examination procedure is an effective enforcement tool. FDIC at 1, 4. Yet of the 6536 examinations it performed in the past three years, only 21 institutions received CRA ratings of 4 or 5. In the face of all the contrary evidence indicating that race is a factor in who gets mortgage money, the FDIC examination process does not seem at all reliable. Even the Federal Reserve Board recognizes that "[d]iscrimination can occur in many subtle ways, and it seldom leaves a visible audit trail." Federal Reserve Board Report at 13. Either all of the recent studies are completely wrong, or the FDIC cannot recognize discriminatory activity. The LCCR generally believes the latter proposition to be true.

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[5] S. Rep. No. 175, 95th Cong., 1st Sess. 33 (1977).

[6] *See* Community Reinvestment Act: Hearings Before the Senate Committee on Banking, Housing and Urban Affairs, 100th Cong., 2d Sess.

[7] *See generally* Citizens' Commission Report at 260-62.

The Office of Thrift Supervision in its Report notes that its loan application register was designed to monitor compliance with the nation's fair lending laws. What if fails to mention, however, is that for all the years it has collected the data it has never performed any analyses of it, at least none that have been made public. The Bank Board has in the past taken the position that its data compilations are not disclosable under the Freedom of Information Act. Although recently aggregate data has been made available, the Bank Board continues to adhere to its position that data collected from individual lenders will not be made available to the public.

The Report submitted by the Board of Governors of the Federal Reserve System is noteworthy principally because of its suggestions for improved efforts to enforce the laws prohibiting discrimination in housing finance. We agree that it is "not practical" for a single bank examiner to perform both safety and soundness, as well as consumer affairs/civil rights examinations, and that the two examinations should be separate. Federal Reserve Board Report at 9. Rather than simply developing separate career paths within the same agency, however, consumer affairs/civil rights examiners should be independent. See Recommendations infra and Citizens Commission Report at 262. We Also favor the Fed's suggestion that Mortgage Review Boards to monitor lender behavior be established in each metropolitan statistical area, although the specifics of such a program need to be worked out.

Nor has HUD been a significant enforcer of the equal lending and housing finance discrimination laws. It has conducted no recent studies or compiled any data relating to its investigation or conciliation of complaints alleging violations of the housing finance provisions of Title VIII.[8] None of HUD's annual reports between 1980 and 1986 make any reference to its investigation and conciliation efforts with respect to housing finance discrimination claims. None of HUD's Voluntary Affirmative Marketing Agreements have involved financial institutions or their trade associations. Equal access to housing credit, therefore, has not been at the forefront of HUD's efforts to enforce the Fair Housing Act.[9] The recent regulations promulgated by HUD with respect to finance discrimination are merely weak restatements of the Fair Housing Act itself, and provide no meaningful guidance to lenders or the public on mortgage lending discrimination matters.

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[8] Letter from Burton Bloomberg, Associate General Counsel for Administrative and General Law, U.S. Department of Housing and Urban Development, to Stephen M. Dane (July 22, 1988).

B. *Until Only Recently, Not the Department of Justice*

Of the more than 300 housing discrimination cases filed by the Department between 1969 and 1978, however, few involved important lending issues such as mortgage and insurance redlining.[10] Prior to 1980 the Department initiated only a handful of mortgage lending discrimination cases, only one of which, the Department's suit against the appraisal industry, resulted in a landmark decision relating to credit issues.[11] The Department did file an amicus brief in a case which established the proposition that racial redlining violates the Fair Housing Act,[12] and an amicus brief in another case which held that a lender violates ECOA by treating unmarried applicants differently than married applicants,[13] but these cases were initiated and ultimately successfully resolved by private plaintiffs.

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[9] Citizens' Commission Report at 260.

[10] U.S. Commission on Civil Rights, *The Federal Fair Housing Enforcement Effort* 57 (1979). Between 1976 and 1982 the Department filed a total of only 12 cases under ECOA. Gorman, *Enforcement of the Equal Credit Opportunity Act*, 37 Bus. Law. 1335, 1345 (1982).

[11] The court in that case held that the prohibitions of Title VIII apply to appraisers of real estate and to appraisal practices. *United States v. American Institute of Real Estate Appraisers*, 442 F. Supp. 1072, 1078-79 (1977), *appeal dismissed*, 590 F.2d 242 (7th Cir. 1978).

[12] *Laufman v. Oakley Building & Loan Co.*, 408 F. Supp. 489 (S.D. Ohio 1976).

The Department's enforcement efforts in the equal credit area did not improve much between 1980 and 1988. The first equal credit case of the Reagan Administration was not filed until October 14, 1982.[14] Between then and November 1, 1987 only a dozen or so additional credit cases have been filed by the Department.[15] It filed its first amicus brief since December, 1980, in a private credit discrimination case only last month. Almost all of the cases filed during the Reagan Administration have been resolved by consent decree. None of the cases filed since 1981 have resulted in any significant interpretation of the equal credit and fair lending laws. The Department lost on the merits one of its few consumer credit cases that did not result in a consent decree.[16]

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[13] *Markham v. Colonial Mortgage Service Co.*, 605 F.2d 566 (D.C. Cir. 1979).

[14] *U.S. v. Avco Financial Services*, C.A. No. Y-82-3032 (D. Md.).

[15] *See* The Attorney General's 1980 Report to Congress pursuant to the Equal Credit Opportunity Act Amendments of 1976, at 3-6; The Attorney General's 1981 Report to Congress Pursuant to the Equal Credit Opportunity Act Amendments of 1976, at 1-4; The Attorney General's 1982 Report to Congress Pursuant to the Equal Credit Opportunity Act Amendments of 1976, at 2-3; The Attorney General's 1983 Report to Congress Pursuant to The Equal Credit Opportunity Act Amendments of 1976, at 2-3; The Attorney General's 1984 Report to Congress Pursuant to The Equal Credit Opportunity Act Amendments of 1976, at 2-4; The Attorney General's 1985 Report to Congress Pursuant to The Equal Credit Opportunity Act Amendments of 1976, at 1-5; The Attorney General's 1986 Report to Congress Pursuant to The Equal Credit Opportunity Act Amendments of 1976, at 1-3; The Attorney General's 1987 Report to Congress Pursuant to The Equal Credit Opportunity Act Amendments of 1976, at 1-5; The Attorney General's 1988 Report to Congress Pursuant to the Equal Credit Opportunity Act Amendments of 1976, at 1-3.

Only since the appointment of a new Chief of the Housing Section of the Department's Civil Rights Division in the summer of 1988 have enforcement efforts increased and the sophistication of the Department's staff in mortgage lending discrimination matters improved to an adequate level. It has recently begun investigations of mortgage lending discrimination throughout the country, and has actively solicited the input of private fair housing groups. We believe the recent enforcement efforts of the current staff of the Housing Section have been vigorous and effective, and we hope that those efforts will continue.

C. Private Fair Housing Groups and Private Citizens Have Been Enforcing the Nation's Mortgage Lending Discrimination Laws

The true "watchdogs" of the lending community with respect to home finance discrimination matters have been private fair housing groups and private citizens. Evidence of this comes from many sources.

First, the vast majority of recent lending studies analyzing HMDA and other available data has been done by private groups, academia, and, most recently, by the news media. Dozens of studies evidencing continuing inequities in the home mortgage financing process now exist, and new ones appear almost monthly.[17] To our knowledge there have been no major studies conducted by any federal agency focusing on mortgage lending discrimination issues for at least a decade.

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[16] *See* Citizens' Commission Report, *supra*, at 259.

Second, most of the litigation challenging discriminatory activity by the mortgage lending industry has been initiated by private citizens and fair housing advocates, not the federal government. All of the recent reported cases involved private litigants, not the United States.

Third, when HUD conducts its training sessions on mortgage lending discrimination matters for its investigators, it relies heavily on the private sector to provide trainers and presenters. HUD apparently does not itself have the staff and/or the expertise to do its own training.

D. Conclusion

The federal government has done little over the past decade to address the very clear mortgage lending discrimination problem in this country. What little enforcement has been done can be attributed to the private sector. The federal government must reassess its priorities in this area and send a clear message to the lending community that the nation's fair lending and equal credit opportunity laws are going to be vigorously enforced to eliminate those problems that still exist.

III. WHAT NEEDS TO BE DONE: OUR RECOMMENDATIONS

A. Simplify the Statutory and Regulatory Scheme

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[17] *See* Citizens' Commission Report, *supra*, at 249-51.

The federal government has over the past 20 years created a confusing maze of equal credit opportunity, fair lending, and community reinvestment statutes and regulations. Different lenders are subject to different statutes and regulations. None of these laws standing alone is comprehensive enough to ferret out all mortgage lending discrimination, and taken together there still exist gaps in coverage, ambiguities in application, and weak enforcement procedures. As the Citizens' Commission on Civil Rights has noted:

> In the late 1960's and 1970's the federal government created a patchwork quilt of equal credit opportunity and fair lending statutes and regulations. Any particular lender suspected of discriminatory lending activity may be subject to some statutes and regulations, but not others. Enforcement mechanisms vary widely. For some statutes, only administrative regulation and enforcement is available, and even then such authority is dispersed among many different federal agencies. The Attorney General has authority to pursue litigation to enforce some laws, but not others. Some federal statutes expressly grant a right to sue to the applicant or other person aggrieved by a discriminatory lending decision. Other laws prohibit one or more types of discrimination but do not provide for an express cause of action to the person aggrieved. Still others are merely recordkeeping or policy statutes designed to inhibit discriminatory lending practices or promote investment in traditionally redlined neighborhoods, without providing for any meaningful penalties for those lenders who fail to comply.18/

The Leadership Conference suggests that Congress adopt a coordinated, comprehensive approach to the problem of discrimination in housing finance. One approach might include

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18. See Citizens' Commission Report, supra at 252.

consolidation of all extant legislation into one statute, and to add provisions that the current scheme lacks. This statute would cover every aspect of the process that leads to the creation and continued existence of a mortgage loan, from the lender's marketing and outreach programs, to pre-application inquiries, through loan processing and underwriting, and continuing through post-closing activities such as the sale and servicing of mortgage loans and the retirement of mortgage loans through, for example, foreclosure. The law should include not only prohibitions against discrimination and unfair treatment, but also should contain affirmative requirements such as data collection, data reporting, easy identification of the location of and access to lender facilities, and other affirmative duties.

A single law that amalgamates all prohibitions and requirements relating to mortgage lending discrimination would be immensely simpler and more efficient than the current confusing framework. Most of the ground work has already been laid in the laws that are currently on the books. Congress need only consolidate into one statute that would relate solely to discrimination in the financing of housing all of the best features of the Fair Housing Act, the Equal Credit Opportunity Act, the Home Mortgage Disclosure Act, and the Community Reinvestment Act.

The strong federal interest in civil rights combined with the federal government's historical involvement in the financial industry make a marriage between the two topics into one act a natural evolutionary step. Whether one is a fair housing advocate or a lender, the appeal to having all of the lender's civil rights responsibilities in one location is the same. The Citizens' Commission on Civil Rights has itself proposed a simplification of the statutory framework.19/

Even more importantly, enforcement powers should be consolidated into one federal agency with the combined civil rights and financial expertise necessary to identify and eliminate barriers to equal credit access. The current Keystone Cop approach, where a dozen or more agencies enforce a single law and adopt different regulations purporting to enforce the same laws (compare the different regulations promulgated by the financial regulatory agencies under the Fair Housing Act) is extremely inefficient and almost incomprehensible to a lay person. Having only one federal agency responsible for enforcing a mortgage lending discrimination law will ensure consistency in the development of substantive guidelines and regulations, procedures for investigation and procedures, and enforcement and penalties. It will also be more efficient and save the government much money in training and in administrative costs if all responsibilities are delegated to one, rather than two or more, agencies.

In addition, the federal enforcers should include a particular emphasis on civil rights enforcement. Given the federal financial agencies' historical reluctance to enforce the

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19. See Citizens' Commission Report, supra, at 263.

fair lending and community reinvestment laws with sufficient vigor, no one of them ought to assume the complete oversight responsibility.

Finally, Congress must make it easier for private interests to enforce the mortgage lending discrimination laws. Simplifying the statutory and regulatory framework would be an important first step in removing much of the mystery and complexity that currently exists in that inhibits private enforcement. The law must be expanded to permit greater access to mortgage lending data from all lenders. Increased knowledge and greater information is critical to the identification of potential mortgage lending discrimination problems. Data currently maintained by the Federal Home Loan Bank Board should be expanded to include all lenders, including mortgage and finance companies. The recent changes to the Home Mortgage Disclosure Act are a positive step in that direction, but more is needed. Third, Congress should appropriate more money for the funding and training of private advocacy groups to encourage activity in this area. It is now too time-consuming and costly for many fair housing groups to become educated in this complex field. Private fair housing and community groups need to hire and train specialized staff to focus on mortgage lending discrimination problems.

B. Conclusion

We appreciate the opportunity to present our views to this Committee, and will be happy to respond further to any questions you may have.

ONE NATION, INDIVISIBLE:

The Civil Rights Challenge for the 1990s

Report of the
Citizens Commission
on Civil Rights

CHAPTER XVI

FEDERAL ENFORCEMENT OF THE FAIR LENDING, EQUAL CREDIT OPPORTUNITY, AND COMMUNITY REINVESTMENT LAWS IN THE 1980s

by Stephen M. Dane

I. Introduction

This paper analyzes the federal government's more recent efforts to enforce those laws and regulations that relate to fair lending, equal access to credit, and community reinvestment. It begins with the proposition that discrimination in credit transactions and the unavailability of much needed credit are still significant problems in this country. It next summarizes the development and current status of the law in this area. It documents the federal government's recent efforts to modify and enforce the fair lending, equal credit, and community reinvestment laws, highlighting both its successes and its failures over the past eight years. Finally, the paper suggests improvements to those laws and their enforcement.

II. Discrimination in Access to Credit: A Statement of the Problem

The history of discrimination in mortgage lending has been well documented, as has the federal government's role in promoting and perpetuating discriminatory mortgage lending practices.[1] When Congress in the 1970s turned its attention to equal credit opportunity issues and discrimination in housing and consumer finance, there was much evidence that minorities, minority neighborhoods, women, and the elderly were subject to a dual housing finance market and suffered from a lack of access to conventional home mortgage credit. Studies conducted by the Comptroller of the Currency and the Federal Home Loan Bank Board indicated the "strong probability of race discrimination in mortgage credit."[2] Evidence presented at hearings before the U.S. Senate Committee on Banking, Housing and Urban Affairs in consideration of the Home Mortgage Disclosure Act of 1975 supplied "ample documentation that credit-worthy persons are sometimes denied loans on sound homes solely because of the location of the property."[3] Studies and testimony from more than a dozen cities showed consistent reluctance on the part of most lenders to make loans in older inner-city neighborhoods.[4] Later studies using data from the mid-1970s confirmed that race was a statistically significant factor in the conventional mortgage markets of many urban areas.[5]

Although the race of the applicant or the racial composition of the neighborhood in which the mortgaged property was located were the most studied and publicized credit problems during this period, they were not the only ones. Testimony in the early 1970s before the National Commission on Consumer Finance noted that single women faced a variety of lender prejudices and were therefore unable to obtain mortgages to buy real estate.[6] In congressional hearings presaging the Equal Credit Opportunity Act of 1976, discrimination against the elderly in consumer credit transactions was the most often cited abuse, despite the fact that in the experience of many creditors their older customers were their best customers.[7]

By 1980 there existed at least 250 studies of mortgage lending patterns conducted by academics, government agencies, and community organizations. An examination of the lending patterns documented by those studies showed a general lack of conventional lending in the inner city, particularly in racially changing areas.[8] A 1980 Federal Trade Commission investigation of mortgage lenders and finance companies found that various subtle forms of discrimination, such as discouraging minorities and others from even applying for credit, appeared to be replacing earlier, more blatant discriminatory practices.[9] An analysis of data collected by the Federal Home Loan Bank Board from FSLIC-insured institutions between October 1980 and June 1983 reveals that blacks were filtered out of the home mortgage process at greater rates than nonminorities.[10]

The most recent access-to-credit studies conclude that race still plays the most significant role in determining who gets conventional mortgage financing. A study of 1983-84 mortgage loan data from the Milwaukee metropolitan area showed that race was "an important factor" in determining the distribution of lending within the area, even after other population and neighborhood characteristics were taken into consideration.[11] A 1984 study by the Woodstock Institute of residential lending patterns in Chicago and its suburbs documented, among other findings, "huge inequalities in the distribution of housing credit throughout the Chicago area that cannot be explained solely by market factors or differences in selling prices."[12] Between 1981 and 1984, neighborhood racial composition directly influenced the distribution of all types of residential lending in Baltimore and all single-family mortgages in its suburbs, even after controlling for normal market mechanisms, such as demand for credit and differences in income levels.[13] A study of New York City lending data showed that applicants from moderate-income, white neighborhoods were three times more likely to receive mortgage loans than applicants from moderate-income, minority neighborhoods. After controlling for all possible other explanations, the authors of the study determined that the only significant variable was race.[14]

Examples of poor lending performance by individual lenders, and the lending industry generally, span the country. Studies conducted in Washington, D.C. and Denver resulted in findings that "race was the strongest predictor of any factor . . . looked at in influencing lending."[15] In Toledo, Ohio, one national bank had only 1.8 percent of its total residential mortgage loan portfolio invested in low-income, minority neighborhoods between 1980 and 1984.[16] In Gary, Indiana, a review of one lender's home mortgage data revealed that it made no mortgage loans in the city between 1980 and 1987. In Tucson, Arizona, the total money made available by one bank for home purchase loans was consistently five times greater in the predominantly white areas of the city than for the minority areas.[17]

Two of the most striking studies come from large metropolitan areas with significant minority populations, Detroit and Atlanta. Both studies, commissioned by major metropolitan newspapers, found highly disparate lending patterns among banks and thrift institutions in white and minority neighborhoods. The Detroit Free Press determined that banks and savings institutions made home loans in the city's white, middle-income neighborhoods at three times the rate of similar black neighborhoods.[18] The study reported that the lending gap between white and black neighborhoods, in the predominantly black city, increased every year from 1982 until it reached a 3-to-1 ratio in 1986, the most recent year complete data were available. Michigan's chief banking regulator, Eugene Kuthy, acknowledged that the findings of the Free Press study were "consistent with trends we have observed in our yearly report on mortgage lending in Michigan."[19]

In Atlanta the lending gap was even larger. White neighborhoods received five times as many home loans from Atlanta's banks and savings and loans as black neighborhoods of similar income, a gap that widened in each year of the study.[20] Even controlling for demand, sales activity, and other economic factors, huge disparities remained. An analysis of applications data revealed that black applicants for home purchase loans were rejected four times as often as whites. One federal savings and loan rejected the loan applications of 36 percent of its black applicants, while rejecting only 10 percent of the white applicants. One bank made thirty-eight times as many loans per structure in white neighborhoods than in comparable black neighborhoods. The study carefully controlled for income and growth, and reviewed patterns over several years, during times of very different national economic conditions and mortgage markets. Yet, nothing explained the different lending patterns as well as race.[21]

The federal government has also noted continuing equal credit problems. The Department of Justice has observed that American Indians who reside on reservations continue to experience problems in obtaining credit on a nondiscriminatory basis, and that many developers and financiers in the resort property industry continue to violate the Equal Credit Opportunity Act (ECOA).[22] For the past two years the Department has noted that evidence of age discrimination in consumer transactions continues to surface.[23] The five financial regulatory agencies have reported declines since 1986 in lender compliance with the technical requirements of Regulation B, the federal government's principal regulation implementing ECOA.[24] As late as 1987, over one-fourth of the regulated institutions studied were in technical violation of the Act or Regulation B, a slightly higher level of noncompliance than reported in 1983 and 1984.[25] In the first quarter of 1988, 130 (37 percent) of the 348 national banks examined by the Comptroller of the Currency for compliance with ECOA were in violation of the Act.[26] The Federal Home Loan Bank Board has seen a steady increase in discrimination complaints since 1982.[27]

There is also growing concern among fair lending advocates that private mortgage insurance companies,[28] and the secondary mortgage market,[29] have adopted policies and underwriting criteria that have a disparate impact on inner-city, minority neighborhoods and discriminate against low-income borrowers.[30] These practices include establishing minimum loan amounts, requiring high minimum downpayments, imposing unduly restrictive credit rating requirements, adopting unnecessary restrictions on the consideration of certain sources of income, arbitrarily considering abandonment ratios in the relevant neighborhood, and other practices.[31] Evidence exists to show that homeowners insurers engage in neighborhood discrimination.[32]

The result of all of this is a clear consensus among fair housing advocates and researchers that "redlining is alive." This belief was consistently expressed at hearings in March, 1988 before the Senate Committee on Banking, Housing and Urban Affairs.[33] The fact that discrimination in housing and consumer finance still exists in the late 1980s suggests an ineffective response by the federal government to remedy what was identified as a problem over a decade ago. This federal failure is due, in part, to a weak and disjointed statutory scheme and, in part, to a lack of commitment by the federal agencies charged with enforcing that scheme, as the discussion that follows demonstrates.

III. Laws and Regulations Prohibiting Discriminatory Lending Practices.

In the late 1960s and 1970s, the federal government created a patchwork quilt of equal credit opportunity and fair lending statutes and regulations. Any particular lender suspected of discriminatory lending activity may be subject to some statutes and regulations, but not others. Enforcement mechanisms vary widely. For some statutes, only administrative regulation and enforcement are available, and even then such authority is dispersed among many different federal agencies. The Attorney General has authority to pursue litigation to enforce some laws, but not others. Some federal statutes expressly grant a right to sue to the applicant, or other person aggrieved, by a discriminatory lending decision. Other laws prohibit one or more types of discrimination but do not provide for an express cause of action to the person aggrieved. Still others are merely recordkeeping or policy statutes designed to inhibit discriminatory lending practices, or promote investment in traditionally redlined neighborhoods, without providing for any meaningful penalties for those lenders who fail to comply. This section will identify those federal statutes, regulations, and executive orders that relate to equal access to credit.

A. Executive Orders 11063 and 12259.

Issued by President Kennedy in 1962, Executive Order 11063 directs federal agencies to ensure that no racial discrimination occurs in financial transactions relating to loans insured or guaranteed by the federal government, that is, FHA and VA loans. Executive Order No. 12259, issued by President Carter in 1980, expanded the coverage of Executive Order 11063 to prohibit discrimination in such transactions based on religion, sex, and national origin, and charged HUD with primary responsibility for coordinating agency implementation of both orders.

Although these executive orders impose nondiscrimination requirements on persons with whom the federal government does business, there exists no private mechanism to enforce them. HUD, and other executive branch agencies, can enforce the orders through informal methods of conference, conciliation, and persuasion, or by canceling agreements, refusing further aid, or otherwise taking appropriate regulatory action against any lender in violation of the orders. Agencies can refer violations of the Orders to the attorney general, who has exclusive authority to initiate civil or criminal actions.

B. Prohibitive Statutes.

1. The Fair Housing Act.

Section 805 of the Fair Housing Act, Title VIII of the Civil Rights Act of 1968, prohibits discrimination in the financing of housing.[34] As is true for the Act generally, any person "aggrieved" by a discriminatory lending practice may assert a cause of action under Sec. 805, regardless of the person's race and regardless of whether the person was the actual applicant for the financing. Thus, in many of the early reported cases the plaintiffs were white applicants seeking loans in minority or integrated neighborhoods.[35]

The new Fair Housing Amendments Act of 1988[36] completely changes the enforcement scheme under Title VIII. Previously an aggrieved individual could either initiate a legal proceeding in any federal or state court of competent jurisdiction or file an administrative charge with the Secretary of the Department of Housing and Urban Development. The Secretary's only statutory responsibility, however, was to investigate the charge of discrimination and "try to eliminate or correct the alleged discriminatory housing practice by informal methods of conference, conciliation, and persuasion."[37] The recent amendments provide for administrative adjudication as an alternative to judicial action, grant the Secretary of HUD specific enforcement authority, and expand the role of the attorney general in all Title VIII litigation.

Despite the fact that the Fair Housing Act is now twenty years old, there are few reported cases construing the specific section prohibiting discrimination in financing. Some of these cases, however, are significant. Most significant are recent cases defining a prima facie case of discrimination under the Act.[38] Although not absolutely clear from a reading of the statute itself, Sec. 805 has been construed to prohibit discrimination based upon the location of the property, that is, redlining.[39] This conclusion is buttressed by federal regulations promulgated under authority of the Act.[40] Federal courts have held that a lender's inconsistent application of its foreclosure policies or procedures is prohibited by the Act.[41] Sec. 805 has been applied to developers and persons or entities other than banks and financial institutions who offer financing for the purchase, construction, or improvement of homes.[42] A companion provision, Sec. 804, has been held to encompass discriminatory appraisal practices[43] and insurance redlining.[44]

One court has narrowly construed Sec. 805, however, not to apply to home equity loans, at least where the purpose of securing the equity loan is unrelated to the improvement, repair, or maintenance of the dwelling.[45] This conclusion is now suspect in light of the recent changes to be made by the Fair Housing Amendments Act of 1988, which includes home equity loans within the coverage of Sec. 805. The Fair Housing Amendments Act also expands the financing discrimination section by expressly prohibiting discriminatory activities of appraisers and secondary mortgage market purchasers.

2. Equal Credit Opportunity Act.

Enacted in 1974 and amended in 1976, the Equal Credit Opportunity Act (ECOA)[46] is both broader and narrower in scope than the Fair Housing Act. It is broader in two significant respects. First, it prohibits discrimination in all credit transactions, not just housing finance transactions. Second, it prohibits discrimination not only on the basis of race, color, religion, national origin, or sex, which are identified in Title VIII, but also discrimination based upon marital status, age, the receipt of income from public assistance programs, or the good faith exercise of rights under the Consumer Credit Protection Act.

ECOA is narrower in scope because it protects only applicants for credit, as distinguished from Title VIII's broad applicability to "any person aggrieved" by a discriminatory lending practice.[47] At least two courts have held in the residential mortgage context that persons or organizations other than the loan applicant do not have standing to assert a claim under ECOA.[48]

Despite its comparatively strong enforcement provisions, ECOA has not been the subject of voluminous public or private litigation.[49] With the exception noted above, however, the Fair Housing Act and ECOA are equivalent enough that such cases construing the Fair Housing Act should be applicable to claims asserted under ECOA. Thus, the requirements of a prima facie case of discrimination are the same under both laws, and any underwriting, appraisal, or financing policy or practice that has an adverse impact on one or more of the statutorily protected groups is a violation of ECOA.[50]

Many federal regulatory agencies are responsible for enforcement of ECOA, and each is authorized to issue regulations relating to such enforcement.[51] The attorney general is authorized to prosecute any matter referred to him by those agencies, or he can bring an action independently of any such referral.[52]

3. *The Civil Rights Acts of 1866 and 1870.*

The Civil Rights Acts of 1866 and 1870[53] state a right to equal treatment in the acquisition of property and the making of contracts. Although enacted in an era largely pre-dating the development and growth of the lending and mortgage industries, the courts have had little difficulty in concluding that these statutes prohibit discrimination in lending practices.[54]

In contrast to the Fair Housing Act and ECOA, however, they prohibit discrimination only on the basis of race; they do not prohibit discrimination based on religion, sex, national origin, marital status, age, or the receipt of public assistance.[55]

They also differ in that a plaintiff must prove discriminatory intent in order to prevail. Moreover, neither the attorney general nor any other federal agency is expressly authorized to initiate any action or otherwise enforce them. Enforcement efforts, therefore, rest solely on private lawsuits brought by victims of discrimination.

4. *Title VI of the Civil Rights Act of 1964.*

Title VI of the Civil Rights Act of 1964[56] prohibits discrimination under any program receiving federal financial assistance. Primary responsibility for enforcement of Title VI rests with each federal agency providing the federal assistance covered by the Act.[57] Although the attorney general is given no independent authority to enforce Title VI, the Department of Justice has interpreted the Act implicitly to authorize the attorney general to commence a civil action upon referral from an enforcing agency.[58]

5. *Title I of the Housing and Community Development Act of 1974.*

Title I of the Housing and Community Development Act of 1974[59] prohibits discrimination based on race, color, national origin, or sex, in the implementation or benefits of any program or activity funded in whole or in part under the Act. HUD and the attorney general have express authority to enforce the Act.[60] It has been held that an unsuccessful applicant for a loan administered under a community development block grant cannot maintain a private cause of action under this statute.[61]

6. *Title V of the National Housing Act.*

Section 527 of the National Housing Act[62] prohibits discrimination on the basis of sex in extending mortgage credit on "federally related" mortgage loans, which by statutory definition makes the Act applicable to virtually all conventional, FHA, and VA loans.[63] Lenders are prohibited by this statute from refusing to consider the combined income of both husband and wife for the purpose of extending mortgage credit to a married couple or either member thereof.

C. Regulatory Statutes.

1. Home Mortgage Disclosure Act.

The Home Mortgage Disclosure Act (HMDA)[64] requires depository institutions to compile and make available, for public inspection and copying, the number and total dollar amount of mortgage loans originated or purchased by that institution during each fiscal year.[65] The Act is solely a recordkeeping and disclosure statute; it does not prohibit redlining or discriminatory lending practices, and therefore does not provide any private cause of action to persons aggrieved by a lender's discriminatory practices. Enacted in 1975, the theory behind the Act was that the public disclosure of geographical lending patterns by depository institutions would "deter" them from practicing redlining.[66] The requirements of the Act are enforced by the federal financial regulatory agencies.

2. Community Reinvestment Act.

The Community Reinvestment Act (CRA)[67] requires federal financial supervisory agencies to assess a regulated institution's record of meeting the credit needs of its community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of such institutions. Like the Home Mortgage Disclosure Act, the CRA was designed to improve the performance of regulated financial institutions in urban neighborhoods.[68] Also like HMDA, the CRA does not provide any express cause of action to those wishing to challenge a regulated institution's compliance with the Act. Some federal agencies, however, have promulgated regulations which permit individuals or community interest groups to challenge, on CRA grounds, a lender's application for approval to expand its service area.[69] This "CRA protest" procedure provides an extremely powerful tool to fair lending advocates wishing to challenge an institution's lending policies and practices.

D. Regulations.

Many regulations relating to the fair lending, equal credit, and community reinvestment laws have been promulgated by the federal financial supervisory agencies.[70] As with the statutory framework on which they are based, these regulations are scattered, overlap each other in some respects, are completely silent in other respects, apply only to certain financial institutions, are enforced by different federal agencies, and, in general, are as confusing to keep straight as are the statutes they enforce.[71] The most noteworthy regulations are those issued by the Federal Reserve Board (Regulation B, the principal regulation implementing ECOA),[72] and the Federal Home Loan Bank Board[73] that proscribe a wide variety of lending practices that do or could discriminate against minorities, minority neighborhoods, women, and other protected groups.[74]

IV. Efforts to Change Legal Standards Since 1980.

The patchwork quilt of federal statutes and regulations relating to equal credit and community reinvestment was created largely between 1968, when the Fair Housing Act was passed, and 1977, when the Community Reinvestment Act was enacted. In the past decade, there have been few legislative, regulatory, or judicial efforts to change the legal standards adopted by the scheme, despite many recommendations for improvement.[75] What few attempts have been made are summarized below.[76]

A. Legislation.

Many attempts were made over the past decade to amend the Fair Housing Act, but none were successful until 1988. Late in that year, Congress passed the Fair Housing Amendments Act[77] which substantially modified and strengthened the enforcement of Title VIII. As mentioned previously, significant substantive changes were made to the financing discrimination provision.

Section 419 of the Housing and Community Development Act of 1987[78] prohibits leaders from establishing minimum mortgage amounts for FHA loans. Fair leading advocates have increasingly voiced concern over the disproportionate impact of such policies on minorities and minority neighborhoods.[79] Unfortunately, the legislation does not address minimum mortgage amounts for conventional loans.

Section 565 of the same Act makes mortgage companies owned by regulated banks and thrifts subject to the disclosure requirements of the Home Mortgage Disclosure Act. Because mortgage companies are not covered by HMDA, they are not required to report the location, amount, and number of mortgage loans they make in metropolitan areas. Sec. 565 ensures that regulated banks and thrifts do not avoid the requirements of HMDA by using separately incorporated mortgage companies to accept mortgage applications. Section 565 also makes the Home Mortgage Disclosure Act permanent.

B. Regulations.

The Department of Housing and Urban Development in the last days of the Carter administration submitted to Congress comprehensive Title VIII regulations that would have assisted in the interpretation of the financing discrimination provisions of Title VIII. As the Citizens' Commission on Civil Rights has already observed, the first action the Reagan administration took with respect to fair housing generally was to recall these proposed regulations.[80]

In the early 1980s the Federal Home Loan Bank Board and the FDIC proposed to eliminate the collection of certain data relevant to the enforcement of Title VIII and the Community Reinvestment Act.[81] The proposals were not adopted after the substantial negative reaction they received.[82]

In 1983 HUD, without explanation, discontinued collecting and reporting data on the location of FHA loans originated by mortgage companies. The elimination of this data from the public domain may be hampering the efforts of serious researchers attempting to document equal credit access problems.[83]

In 1985 the Federal Reserve Board issued revisions to Regulation B and published an official staff commentary to assist creditors in complying with the regulation.[84] Among the notable improvements were an expanded definition of the term "applicant" that grants legal standing to guarantors of loans when a creditor has improperly required their signatures. The revisions also imposed additional data collection requirements.[85] The Board failed to adopt proposed changes that would have extended the technical requirements of Regulation B to business credit transactions and to lease transactions.[86]

In 1987, the Federal Reserve Board amended its Official Staff Commentary to make clear that lenders are not required by Regulation B to collect data regarding home equity or home improvement loans.[87] In August, 1988 the FDIC followed the Fed's lead by narrowing its regulatory definition of "home loan" for data collection purposes so that the lenders it regulates no longer need to collect data regarding home equity and home improvement loans.[88] The banking community generally favored the FDIC's move, while community advocacy groups and another agency of the federal government opposed it.

The omission of home improvement and home equity loans from the data collection regulations, after ten years of obtaining such data by some agencies, is extremely unfortunate. The U.S. Commission on Civil Rights in 1979 praised the FDIC for its comprehensive data collection regulations and contrasted its collection of home improvement loan data with the Federal Reserve Board's failure to do so.[89] Home equity loans now rate as the fastest growing consumer loan product in the country. Congress has declared that discrimination in the processing of such loans is prohibited by the Fair Housing Act, and data regarding lender distribution and treatment of such loans by racial, neighborhood, and gender categories would be very helpful to the regulators and others who monitor lender behavior. Moreover, there is some evidence that race plays a factor in home improvement lending.[90]

C. Case Law.

As noted earlier the case law interpreting Title VIII, ECOA, and other credit discrimination laws is relatively sparse.[91] There have been no reported efforts by the federal government to modify, supplement, or pull back from the case law that currently exists. Indeed, as demonstrated in the next section, the Department of Justice has engaged in little meaningful equal credit litigation at any time.

V. Failures of Enforcement

The patchwork quilt of federal statutes, regulations, and executive orders that are designed to prohibit discriminatory lending practices is enforced by a labyrinthine network of federal agencies. In many areas the enforcement powers of those agencies overlap. In other areas the enforcement scheme is so weak as to allow no enforcement at all. This section will highlight the failures and successes of federal enforcement of these laws over the past eight years.

A. Department of Justice.

Of the statutes identified in Section III above, the Attorney General of the United States is empowered to enforce the Fair Housing Act, the Equal Credit Opportunity Act, Title VI of the Civil Rights Act of 1964, and Executive Order No. 11,063.

The Department's efforts to enforce these equal credit laws have been analyzed in detail before.[92] Prior to 1980 the Department was praised for the impressive quality of its litigation record in cases involving discrimination in apartment rentals and racial steering.[93] Of the more than 300 housing discrimination cases filed by the Department between 1969 and 1978, however, *few* involved important lending issues such as mortgage and insurance redlining.[94] Prior to 1980 the Department initiated only a handful of mortgage lending discrimination cases, only one of which, the Department's suit against the appraisal industry, resulted in a landmark decision relating to credit issues.[95] The Department did file an amicus brief in a case which established the proposition that racial redlining violates the Fair Housing Act,[96] and an amicus brief in another case which held that a lender violates ECOA by treating unmarried applicants differently than married applicants,[97] but these cases were initiated and ultimately successfully resolved by private plaintiffs. The Department lost repeatedly, trying to persuade the courts that the attorney general has standing under ECOA to recover damages on behalf of victims of discrimination,[98] and lost arguments regarding removal jurisdiction that it made in an October, 1980 amicus brief filed in a private case.[99]

The Department's enforcement efforts in the equal credit area have not improved much in the last eight years. The first equal credit case of the Reagan administration was not filed until October 14, 1982.[100] Between then and November 1, 1987 only a dozen or so additional credit cases have been filed by the Department.[101] It has not filed an amicus brief in a private credit discrimination case since December 4, 1980.[102] Almost all of the cases filed during the Reagan administration have been resolved by consent decree.[103] None of the cases filed since 1981 have resulted in any significant interpretation of the equal credit and fair lending laws. The Department lost on the merits one of its few consumer credit cases that did not result in a consent decree.[104]

The Department can claim some positive achievements since 1980. It prevailed in the one equal credit case that did go to trial. It filed more credit cases (six) in 1986 than in any other single year since the Fair Housing Act and ECOA were passed. It has devoted significant attention to equal credit problems experienced by American Indians.[105] It regained some lost ground on the issue of standing by obtaining a district court decision holding that the Federal Trade Commission, acting through the attorney general, has authority under ECOA to seek civil penalties and consumer remedies.[106]

There are many possible explanations for the Department's generally unimpressive record in prosecuting lending discrimination claims.

First, the Department's lack of subpoena power under Title VIII and ECOA may impede the investigation of lending discrimination claims. The Department itself has recognized that the lack of general subpoena power can be a major problem in racial redlining and other lending discrimination cases.[107] The Department also apparently continues to shun the use of investigative techniques that have become standard in the fair housing field, such as testing and statistical analysis of data, to identify potential finance discrimination cases.[108]

Second, the Department rarely receives referrals from other federal agencies charged with equal credit enforcement authority.[109] In 1980 and 1981 the Department expressed its "concern" with the relatively small number of credit discrimination referrals it was receiving, despite the high incidence of violations noted by other agencies.[110] Between 1978 and 1988, the Department reported only one matter referred to it by another agency (the FTC) under the authority of Sec. 706(g) of ECOA.[111]

Third, the internal organization of the Department does not seem conducive to a vigorous enforcement program in the equal credit area. As of September 20, 1978 the Department had only eight attorneys on its staff responsible for credit cases.[112] In April 1979, the Housing and Credit Section of the Civil Rights Division was merged with the Education Section to form the General Litigation Section.[113] Staffed with forty-three lawyers and thirty-two paralegal and clerical employees, the mission of the section was to attack interrelated problems--such as housing discrimination and school desegregation--on a broad basis rather than piecemeal.[114] There was no specialization; each staff member was expected to have credit responsibilities. In November 1983, credit responsibilities were split off from the General Litigation Section and were given to a newly-formed Housing and Civil Enforcement Section.[115] The change in structure was designed to establish smaller litigation groups that would focus on discrete problems.[116] The seventeen lawyers and thirteen paralegal and clerical employees originally assigned to it were responsible for enforcing not only the fair housing and equal credit laws, however, but also federal statutes prohibiting discrimination in public accommodations and in federally funded municipal services.[117]

Thus, there appears to be no consistent, clearly focused method of dealing with equal credit matters. Individual staff members in the Housing and Civil Enforcement Section work on all statutes for which the Section has responsibility.[118]

There has been no change in the total size of the Section's staff since 1983; it still has an authorized strength of only eighteen attorneys and twelve paralegals and support staff.[119]

Without an increase in staff, or a more focused approach to credit issues, the chances are slim that the Department can significantly increase its enforcement efforts in the field.

Fourth, the Reagan administration has demonstrated less vigor than previous administrations in its enforcement of the nation's civil rights laws.[120] Of particular importance to fair lending litigation is the administration's abandonment of the "effects" test under Title VIII.[121] This test is of critical importance in the mortgage lending field where facially neutral loan underwriting guidelines and pricing policies may have a disparate impact on minorities and minority neighborhoods, even though an intent to discriminate may not be apparent.

Finally, the administration has consistently espoused a hands-off approach to vigorous regulation of the financial industry. This is evidenced by its push for deregulation of the financial industry in the early 1980s and by the failure of the federal supervisory banking agencies to enforce the equal credit and community reinvestment laws subject to their jurisdiction.[122]

It would be hard to fault the Department if indeed there were no indications that lending discrimination still exists.The evidence, however, is to the contrary.[123] Private plaintiffs have identified, and successfully litigated, lending discrimination cases. There is no reason why the Department of Justice with its superior resources cannot do so as well.

B. Department of Housing and Urban Development.

Prior to the recent enactment of the Fair Housing Amendments Act of 1988, the Department of Housing and Urban Development had little meaningful authority to enforce any of the fair lending or community reinvestment laws. Rather, HUD's only statutory responsibility in the equal credit area was to receive and investigate housing finance discrimination claims and "try to eliminate or correct the alleged discriminatory housing practice by informal methods of conference, conciliation, and persuasion."[124] The secretary was not even permitted to engage in these conciliatory activities if the housing finance complaint arose in a jurisdiction with a state or local fair housing law substantially equivalent to the Fair Housing Act.[125]

Thus, HUD has not been a significant player in the enforcement of equal lending and community reinvestment laws, even Title VIII. It has conducted no recent studies or compiled any data relating to its investigation or conciliation of complaints alleging violations of the housing finance provisions of Title VIII.[126] None of HUD's annual reports between 1980 and 1986 even mention its investigation and conciliation efforts relating to complaints of housing finance discrimination. None of HUD's Voluntary Affirmative Marketing Agreements have involved financial institutions or their trade associations. Equal access to housing credit, therefore, is not at the forefront of HUD's efforts to enforce the Fair Housing Act.

HUD could have made a significant contribution to the interpretation of Title VIII's prohibition against discrimination in the financing of housing if it had issued comprehensive regulations relating to that topic. The promulgation of regulations by other federal agencies in their particular areas of expertise has been recognized as an invaluable tool in the enforcement and interpretation of civil rights legislation.[127] HUD did submit Title VIII interpretative regulations to Congress in 1980, but those regulations were withdrawn soon after the Reagan administration took control of the White House. Fortunately, other federal regulatory agencies, in particular the Federal Reserve Board through Regulation B,[128] and the Federal Home Loan Bank Board in its nondiscrimination regulations,[129] have adopted strong, comprehensive fair lending regulations that have filled the gap left by HUD's inactivity in the housing finance area.

HUD can substantially improve its enforcement efforts after the Fair Housing Amendments Act of 1988 takes effect. Whether it does so will depend upon the commitment of the new administration to fair housing matters, generally, and to equal access to credit in particular.

C. Financial Supervisory Agencies.

Five federal regulatory agencies, with general supervisory responsibility over financial institutions, enforce certain fair lending and community reinvestment laws: the Board of Governors of the

Federal Reserve System, the Federal Home Loan Bank Board, the Federal Deposit Insurance Corporation, the Comptroller of the Currency, and the National Credit Union Administration. These agencies are charged with enforcement of the Equal Credit Opportunity Act,[130] the Home Mortgage Disclosure Act,[131] and, except for the National Credit Union Administration, the Community Reinvestment Act.[132]

1. Community Reinvestment Act.

None of the financial regulatory agencies have vigorously enforced CRA.[133] Prior to enactment of CRA, the agencies focused their efforts exclusively on monitoring the financial "safety and soundness" of the institutions they regulated, and generally ignored those institutions' commitment to neighborhood reinvestment.[134]

Despite the enactment of strong fair lending laws and Congress' clear expression of federal policy that discriminatory lending practices should be eliminated, the federal financial supervisory agencies did little or nothing throughout most of the 1970s to implement or enforce this national priority.

The Senate Banking Committee (in 1977) harshly criticized the regulatory agencies for not promulgating anti-redlining regulations.[135] Indeed, during the congressional hearings that led to passage of the CRA, the agencies discounted any evidence that redlining existed and, although they acknowledged that lenders were not meeting community credit needs, resisted the philosophy of CRA.[136] Only after being sued by a coalition of civil rights groups did the Comptroller of the Currency, the Federal Reserve Board, the Federal Deposit Insurance Corporation, and the Federal Home Loan Bank Board promulgate regulations to enforce and monitor compliance with Title VI, the Fair Housing Act, ECOA, and the Community Reinvestment Act.

At first, it appeared as though the federal regulators would wield their new CRA enforcement duties with sufficient vigor to squarely address the problem of credit unavailability in urban neighborhoods. The first decision by a federal supervisory agency to deny a bank's application on CRA grounds is reported to have "sent shock waves through the banking community."[137] Several early rulings by the Comptroller of the Currency hinted at an active enforcement program.[138] Although not required by the statute itself, federal agencies promulgated regulations which permit individuals and community interest groups to challenge on CRA grounds a lender's application for approval to expand its service area.[139] This "CRA protest" procedure provides an extremely powerful tool to fair lending advocates wishing to challenge an institution's lending policies and practices. Indeed, use by community organizations of the CRA protest procedure has been the single major method of enforcement of the federal policy against discriminatory lending practices affecting older, minority, urban neighborhoods.[140]

In recent years, however, the CRA enforcement efforts of the regulatory agencies have been harshly criticized. Studies by the General Accounting Office, a house subcommittee, and others, found that administrative enforcement efforts were not being used regularly and effectively to promote CRA compliance.[141]

In hearings before the Senate Committee on Banking, Housing, and Urban Affairs conducted in March, 1988, fair housing advocates and researchers were united in their criticism of the financial regulatory agencies.[142] Statistics submitted by the agencies and their critics demonstrated that the CRA rating system[143] used by the agencies is misleading, ineffective, and arbitrary.[144] The agencies' examination procedures were shown to be ineffective because CRA and fair lending issues are not deemed to be important, examiners are not adequately trained in CRA and fair lending matters, too few resources are allocated to the CRA portions of examinations, and the examinations are conducted too infrequently.[145] Agency procedures to evaluate CRA challenges to a lender's application to expand its service area are weak, inherently deficient, and often inconsistently followed.[146]

Despite their poor record and the many examples of weak enforcement, the federal regulatory agencies argue that (1) they are adequately enforcing the Community Reinvestment Act and its implementing regulations and (2) there is no redlining or lending discrimination "problem" in the country. This latter belief is clearly expressed in statements made by the regulators during the 1988 CRA Oversight Hearings. The Comptroller of the Currency, for example, believes that "banks historically have helped to meet local community credit needs, consistent with safety and soundness requirements, and they continue to do so."[147] The FDIC expressed its belief that "FDIC-supervised banks are in substantial compliance with the requirements of the CRA and Part 345 of the FDIC's regulations."[148]

These comments perhaps underscore the folly of having CRA and equal credit compliance monitored by regulators whose interests are too closely tied to the institutions they regulate. For example, examiners and supervisory staff work for the regional Federal Home Loan Banks. The boards of directors of the regional Banks, however, are filled with officials of the savings and loans institutions that are being examined. Moreover, the agencies are responsible for insuring deposits, supervising loan activities, and generally insuring the safety and soundness of depository institutions. Thus, the health and welfare of the industry itself is the agencies' primary concern, not the elimination of discriminatory policies and practices.

All of this is not to say that enactment of the Community Reinvestment Act was a mistake, or that some of its purposes have not been fulfilled. To the contrary, in contrast to attitudes of ten years ago, both lenders and the agencies now readily acknowledge that lenders have an affirmative obligation to meet the credit needs of low- and moderate-income neighborhoods and to provide access to adequate credit in those neighborhoods. As one commentator has cogently observed, in the ten years since the CRA was passed "the banking officials and regulators who, prior to 1977, resolutely and unapologetically denied that they had any responsibilities to serve the credit needs of local communities, are now in the position of explaining how they are doing enough to fulfill those responsibilities."[149]

Moreover, the use by private community organizations of the CRA protest procedure has resulted in a tremendous amount of reinvestment in traditionally redlined or disinvested neighborhoods. Experts have estimated that since CRA was passed, private community organizations have used the Act and its protest procedure to negotiate almost $5 billion in additional credit to those neighborhoods.[150] More than once it has been observed that the driving force behind the successful implementation of the CRA's purposes has been activist community organizations.[151]

The point to be made, however, is that the federal financial supervisory agencies, which, rather than community organizations, are charged with the primary statutory responsibility for enforcement of the Community Reinvestment Act, are not fulfilling their statutory obligations.

2. *Equal Credit Opportunity Act.*

The federal agencies' efforts to enforce compliance with ECOA appear to be better than under CRA. For example, both the Federal Home Loan Bank Board and the Federal Reserve Board have promulgated nondiscrimination requirements that are broad, comprehensive and strong. Some of the agencies--particularly the Federal Reserve Board and the Federal Trade Commission--regularly issue cease and desist orders, and initiate enforcement actions against lenders who are found in violation of ECOA. For example, between 1980 and 1987 the agencies initiated approximately forty formal enforcement proceedings, including cease and desist orders, against lenders found to be in violation of ECOA.[152]

The Federal Trade Commission appears to be the most vigorous enforcer of ECOA.[153] It regularly conducts investigations into practices that it considers to be serious violations of ECOA,[154] and has initiated one or more enforcement proceedings each year since 1982.[155] In 1984 the FTC brought the first enforcement action under ECOA to challenge restrictive loan terms to the elderly on the grounds that the restrictions were not reasonably related to creditworthiness.[156] The FTC has also implemented and regularly uses statistical analysis and "testing" to ferret out ECOA violations.[157]

VII. Emerging Issues and Challenges/Recommendations

This section identifies the emerging issues and challenges the next administration must face if it truly desires to eliminate remaining artificial barriers to credit in housing and consumer finance transactions. This section makes specific recommendations for improving the present statutory, regulatory, and enforcement framework so that the new administration can more effectively enforce the nation's policy against discriminatory lending practices.

A. Simplify the Statutory Framework and Place Enforcement Authority In One Federal Agency.

Congress has, over time, built an extremely confusing and complicated statutory framework in its effort to eliminate discriminatory lending practices. Federal enforcement of the fair lending and community reinvestment laws is expensive, inefficient and, for the most part, ineffective.

The current scheme must be simplified. This could be accomplished by, for example, enacting legislation that amalgamates into one statute relating solely to discrimination in the financing of housing all of the best features of the Equal Credit Opportunity Act, the Home Mortgage Disclosure Act, the Community Reinvestment Act, the financing section of the Fair Housing Act, and related provisions from other laws and executive orders. The Equal Credit Opportunity Act itself would remain largely intact, but could be limited to consumer transactions only. In this way two laws could do the same job that half a dozen do now, and there would be no overlap.

Regulatory and enforcement authority should be placed in one federal agency, or two if consumer credit and home financing are treated separately by statute. Given the federal financial agencies' historical reluctance to enforce the fair lending and community reinvestment laws with sufficient vigor, the Department of Housing and Urban

Development is the most logical choice to enforce any and all laws relating to home finance discrimination and community reinvestment. The Federal Trade Commission could be charged with responsibility for enforcing any laws relating to discrimination in consumer credit transactions. All applicable substantive, procedural, and reporting regulations, which hopefully would include at least those currently on the books, should be promulgated by only one or two of these enforcing agencies. This system would substantially improve the current legal framework by eliminating the redundancies, inefficiencies, gaps, and complexities that now exist.

There are other alternatives to be sure, but some unification is imperative. Even if a radical restructuring is not feasible, the existing scheme can and must be improved. Some specific suggestions follow.

B. Expand Statutory Coverages.

Because of the patchwork nature of the federal statutory scheme relating to credit discrimination issues, particularly discrimination in the financing of housing, there are many gaps and ambiguities in coverage, both with respect to the type of activities covered and with respect to the institutions subject to the laws. What follows are specific proposals for filling the major statutory gaps that remain.

1. The Fair Housing Act.

Even with recent changes implemented by the Fair Housing Amendments Act of 1988, there are some aspects of the Fair Housing Act, as it pertains to discrimination in home financing, that need to be addressed.

The advertising and marketing efforts of a lender can have a profound impact on the extent to which its loan products are made available to the classes of persons protected by the equal lending laws, yet it is unclear whether a lender's advertising or marketing programs that are directed primarily to white, upper-income applicants as opposed to minority, lower-income persons violate the Fair Housing Act.[158]

Accordingly, the Act should be amended to make clear that lenders have an affirmative obligation to market their residential real estate related products to minorities and minority neighborhoods.

Second, it remains unclear whether the Act prohibits discriminatory practices of private mortgage and homeowners insurers. Federal courts are currently split on the issue of whether geographic redlining by hazard or fire insurance companies is a violation of the Act. Many states now expressly prohibit such discrimination in the sale of fire or homeowners insurance.[159] Fair housing advocates believe that private mortgage insurance companies have imposed artificial and discriminatory underwriting restrictions on mortgage insurance applicants. The Act should therefore be amended to expressly prohibit discriminatory policies, practices, and activities of private mortgage and homeowners insurers.

2. Home Mortgage Disclosure Act.

The Home Mortgage Disclosure Act has proved to be an invaluable tool in identifying discriminatory lending patterns. Its two major flaws, however, must be corrected.

The first weakness of HMDA is that it applies only to depository institutions, and does not apply to mortgage companies that are unaffiliated with such institutions. Except for the fact that mortgage companies have not been historically regulated by the federal government, there is no reason why they should be exempt from HMDA's reporting requirements. HMDA's purposes are to deter redlining practices and to identify those lenders who are engaged in discriminatory practices. Including mortgage companies within the Act's coverage is consistent with these purposes. Moreover, with the recent expansion of the Act by Congress to include mortgage companies that are affiliated with depository institutions, there now exists a legislative distinction in the mortgage banking industry that is artificial, unnecessary, and competitively inhibiting. The Act should therefore be amended to include all mortgage companies.

The second major flaw of HMDA is that it does not require the collection, compilation, or reporting of applications data. Only the Federal Home Loan Bank Board collects data on applicant flow. Such data is necessary to measure properly each institution's loan approval rate in the protected categories and to measure the demand for mortgage loans, both throughout the community and on an institution-by-institution basis. Nor does HMDA require the compilation and reporting of loan file data, such as length of employment, credit ratings, income to debt ratios, and other important underwriting factors. Such data should also be made available, subject to protecting the confidentiality of the identity of mortgage loan applicants.

These refinements to HMDA will significantly improve the amount of data publicly available to analysts, researchers and watchdog groups. They will also clarify the extent of the mortgage lending problem in the country and identify which particular lenders are engaged in discriminatory practices.

3. *Community Reinvestment Act.*

As with HMDA, the Community Reinvestment Act does not apply to mortgage companies because they are not depository institutions. There is no reason, however, to exclude mortgage companies from the reach of CRA. They, like depository institutions, should be obligated to meet the credit needs of their communities. Enforcement of CRA against mortgage companies could be delegated to the Federal Trade Commission, which currently enforces ECOA as it applies to mortgage companies.

In addition, to assist and monitor the regulators and to acknowledge the significant importance of private community involvement in the enforcement of CRA, an additional enforcement mechanism should be made available to community groups. Currently the only private means of "enforcing" CRA is to await the filing of a lender's application for approval with a federal financial supervisory agency, and then to challenge that application through the CRA protest procedure. There is neither a method available to appeal the federal agency's decision nor a method of challenging a lender's CRA performance in the absence of an application.

This shortcoming of the CRA can be remedied in a number of ways. The first option is to provide a private cause of action to any bonafide community organization that wishes to challenge a lender's CRA performance. This could be done either through an administrative enforcement scheme or through the courts. Another option is to provide protesting community groups with a right to appeal a federal agency's decision. Once again, the appeal can be either an administrative one to a special appeals panel within the agency itself or directly to a court. Whatever method is eventually adopted, there should be a provision explicitly providing legal standing to community or fair lending advocates who participate in the process.

Another improvement suggested by fair lending advocates to the Act itself is a prohibition against any residential mortgage loan underwriting policy, pricing policy, or product that has a discriminatory effect on low income applicants, such as minimum loan amounts or the tiering of interest rates or closing costs based upon the size of the loan. Such policies are already prohibited by Title VIII and ECOA to the extent that they have an adverse impact on protected groups, but those low-income persons who do not fall within any of the protected categories cannot claim the protection of those laws. Yet the Community Reinvestment Act is specifically designed to protect the interests of all low-income persons, not just those covered by the nondiscrimination statutes.

B. Regulators and Regulations.

In addition to the legislative issues and needs identified above, many perceived defects in federal agency enforcement efforts must be addressed.

1. *Department of Justice.*

The Department has lacked vigorous involvement in litigation regarding equal credit issues. In addition to the statutory impediments to these efforts (such as a lack of subpoena power under Title VIII), there are intradepartment deficiencies that ought to be remedied. First, the amount of staff dedicated to equal credit issues should be increased. Second, the Department should return to its former division of labor, whereby a separate credit subsection handles only credit-related matters. Credit discrimination is more complex and requires a good deal of training and expertise, more so than in other fair housing fields. It would appear to be more efficient to have specialists dedicated to this particular subject area. Third, the Department should actively use the investigative tools used by private fair lending advocates to identify lending discrimination, including the collection and analysis of lending data and the use of testing. The Department should be able to work closely with other federal regulatory agencies that have access to such data or who have testing programs in place.

2. Department of Housing and Urban Development.

It is anticipated that with passage of the new Fair Housing Amendments Act of 1988 HUD will be able to increase its enforcement efforts in all areas of housing discrimination, including finance discrimination. Interpretative regulations must be sensitive to the issue that discrimination in financing is more difficult to detect and to challenge than discriminatory rental, sales, and steering practices. The regulations the federal financial supervisory agencies promulgated under the authority of Title VIII, ECOA, HMDA, and CRA should be of some assistance to HUD, but those regulations are not sufficient in themselves because they apply only to lending institutions subject to federal financial supervision. Other entities subject to Title VIII and ECOA, such as unaffiliated mortgage companies and finance companies, need further specific direction in the form of regulations from HUD.

3. Federal Financial Supervisory Agencies.

Many suggestions have been made for improving the non-discrimination and community reinvestment enforcement efforts of the federal financial supervisory agencies. These suggestions, along with others that have application broader than just CRA, include the following:

- Regulations need to be updated. Most of the present regulations were promulgated almost a decade ago before the effects of deregulation were felt. With the exception of the Federal Reserve Board's regular evaluation of Regulation B, none of the other regulations have been reviewed to any great extent. This is probably an indication of the relatively low priority nondiscrimination in lending has received by the agencies over the past decade. Although some of the regulations are fairly strong, particularLy Regulation B and those promulgated by the Federal Home Loan Bank Board, they should nevertheless be reviewed, cleaned up, and, if necessary, strengthened.

- The CRA ratings system must be revised and ratings made public. In 1983, the Citizens Advisory Council of the Federal Reserve Board unsuccessfully recommended that the system be overhauled. The current ratings system is generally perceived as meaningless since almost all examined institutions are given high ratings, and the ratings themselves are kept secret from the public.

- The CRA examination process must be improved. The examination process as it relates to an assessment of a lender's compliance with the CRA is deficient. The current process emphasizes too heavily safety and soundness concerns and virtually ignores nondiscrimination and community reinvestment performance. As with ratings, the results of examinations should be made public, with respect to CRA issues.

- CRA protest procedures should be standardized and improved. Each agency has its own CRA protest procedure, often inconsistently followed. Longer periods for public comment are needed, and public hearings should be utilized more frequently.
- "Testers" should be used to monitor compliance. Testing has proven to be an invaluable tool for the identification and investigation of other forms of prohibited discrimination. The Federal Trade Commission utilizes testing procedures to check for violations of ECOA. There is no reason why the financial supervisory agencies cannot establish a testing program.
- Data collection procedures and improved data analysis should be implemented. The agencies' data collection procedures should be reviewed to insure that the agencies are collecting all relevant information from the regulated institutions. What data the agencies do have should be exhaustively analyzed, used to identify lender violations or shortcomings, and made public. The Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Federal Reserve Board should collect and analyze the same data that the Federal Home Loan Bank Board currently collects, particularly applications data. The agencies should also aggregate the data collected from each SMSA to determine if, and identify which, urban neighborhoods in the SMSA are not having their credit needs met.
- Advisory boards should be established to assist the agencies. One of the long-standing criticisms of the federal financial supervisory agencies' enforcement of nondiscrimination laws is the incestuous relationship between the agencies and the institutions they regulate. Hence, the agencies themselves should be watched by consumer advisory panels who can make specific recommendations with respect to the enforcement of nondiscrimination and community reinvestment laws. The Citizens Advisory Council performs such a valuable function for the Federal Reserve Board. Many members of the CAC have expressed strong support for the wider use by other regulatory agencies of advisor groups similar to the CAC.[160]

C. Private Enforcement.

The strongest efforts to enforce the nation's credit discrimination and community reinvestment laws have come from private individuals, fair lending advocates, and neighborhood community groups. Although the focus of this paper has been on the strengths and weaknesses of federal enforcement of those laws, impediments to private enforcement do exist. Those impediments have been identified (in part A above) in the discussion of each of the equal credit and community reinvestment statutes. Continued vigorous enforcement in the private sector depends heavily on those suggested improvements being made.

ENDNOTES

Chapter XVI

1. *See, e.g.*, J. Abrams, "Forbidden Neighbors--A Study of Prejudice In Housing" (1955); *U.S. Commission on Civil Rights, Housing* (1961); Comment, "Mortgage Discrimination: Eliminating Racial Discrimination in Home Financing Through The Fair Housing Act of 1968," 20 *St. Louis U.L.J.* 139 (1975); Bradford, "An Analysis of Underwriting and Appraisal Practices and Their Impact on Credit Availability," 3 *Real Estate Issues* 1 (1978); Bradford, "Financing Home Ownership: The Federal Role in Neighborhood Decline," 14 *Urb. Aff. Q.* 313 (1979); Federal Reserve System Compliance Handbook, Part I, Section 1 (1979); Potomac Institute, Lender's Guide To Fair Mortgage Policies 7-10, 17-24 (1980); Citizens' Commission on Civil Rights, A Decent Home: A Report on the Continuing Failure of the Federal Government To Provide Equal Housing Opportunity 7-11 (1983); Bradford, Report on the Role of the Veteran's Administration in Causing Rapid and Massive Racial Resegregation (1984).
2. S. Rep. No. 589, 94th Cong., 2d Sess. 3, *reprinted in* 1976 U.S. Code & Cong. & Admin. News 403, 405.
3. S. Rep. No. 187, 94th Cong., lst Sess. 1 (1975).
4. *Id.* at 2, 5-8.
5. *See, e.g.*, Shear & Yezer, "Discrimination in Urban Housing Finance: An Empirical Study Across Cities," 61 *Land Economics* 292, 300, 301 (1985); R. Schafer & H. Ladd, *Discrimination in Mortgage Lending* 7-8, 60, 134, 182-84, 222-24, 287-99 (1981).
6. Federal Reserve System Compliance Handbook at I.1.22 (1979); *see* R. Schafer & H. Ladd, *supra* note 5, at 6-7, 377 n.8; Ladd, "Equal Credit Opportunity: Women and Mortgage Credit," 72 *Am. Econ. Rev.* at 166-70 (1982); National Council of Negro Women, Inc., Women & Housing: A Report on Sex Discrimination in Five American Cities 59-73 (1975). Some lenders, for example, worried that single women could not perform the necessary repairs to maintain the property, but made no such assumptions with respect to men. Some lenders would provide mortgages to women only if a male cosigner was available, no matter what the financial status of the male might have been. Often lenders refused to recognize a wife's income, or would give it only half credit, a practice apparently motivated by the presumption that women would be likely to become pregnant and terminate their employment. Indeed, some banks required letters from doctors or affidavits concerning birth control methods, sterility, and intentions regarding abortions. Creditors were often unwilling to extend credit to a married woman in her own name. Creditors often required a single woman who had been granted credit to reapply for credit in her husband's name upon marriage. Women who were divorced or widowed encountered difficulties reestablishing their own credit. Federal Reserve System Compliance Handbook at I.1.22 (1979).
7. S. Rep. No. 589, 94th Cong., 2d Sess. 3, *reprinted in* 1976 U.S. Code Cong. & Admin. News 403, 405.
8. Bradford, Report on the Role of the Veterans Administration in Causing Rapid and Massive Racial Resegregation 16-17 (1984).
9. Board of Governors of the Federal Reserve System, 67th Annual Report, at 179-80 (1980).
10. For example, the percent of mortgage loans to blacks decreased from 4.1 percent in 1980 to 2.9 percent by June of 1983. This latter figure is striking when one considers that blacks own 7.2 percent of all owner-occupied housing according to the 1980 census. The same data shows that minorities were less likely to apply for loans, the applications that were made were less likely to be acted upon, and the applications were more likely to be rejected.
11. G. Squires & W. Velez, *Redlining and the Destabilization of Minority and Racially Mixed Communities* 9-11 (undated).
12. Woodstock Institute, "Partners in Need: A Four-Year Analysis of Residential Lending in Chicago and its Suburbs," at v (1986). *See also* Schlay, "Not in That Neighborhood: The Effects of Population and Housing on the Distribution of Mortgage Finance Within the Chicago SMSA," 17 *Soc. Sci. Res.* 137 (1988).
13. A. Schlay, "Maintaining the Divided City: Residential Lending Patterns in the Baltimore SMSA," 59 (1987).

14. *New York Times*, Dec. 5, 1988.

15. Community Reinvestment Act: Hearings Before the Senate Committee on Banking, Housing, and Urban Affairs, 100th Cong., 2d Sess. 124 (testimony of Elspeth Revere) (hereinafter 1988 CRA Hearings); *see* Woodstock Institute, "Vista of Opportunity: An Analysis of 1983 and 1984 Residential Lending in the Denver/Boulder SMSA," 35-36 (1987); Woodstock Institute, "Where the Money Flows: Lending Patterns in the Washington, D.C.-Maryland- Virginia SMSA," 91-92 (1985). *See* also I. Goldstein, *The Persistent Significance of Race: A City Suburb Comparison of Mortgage Lending in the Philadelphia Metropolitan Area* (1987).

16. Toledo Fair Housing Center, Mortgage Lending Report: 1980-1984 at 8, 29 (1986).

17. 1988 CRA Hearings, *supra* note 15, at 54-56.

18. *Detroit Free Press*, July 24, 1988, at 1.

19. *Id.*

20. *Atlanta Constitution*, May 1, 1988, at 1.

21. *See* 1988 CRA Hearings, *supra* note 15, at 110-11 (testimony of Calvin Bradford).

    There are critics who still refer to redlining and mortgage discrimination as a "myth." In the late 1970s, the banking industry and federal regulators commissioned studies that purported to "explode" the myth of racially discriminatory redlining. *See*, e.g., Benston, Horsky, & Weingartner, *An Empirical Study of Mortgage Redlining*, Monograph 1978-5; Guttentag & Wachter, *Redlining and Public Policy*, Monograph 1980-1; King, *Discrimination in Mortgage Lending: A Study of Three Cities*, Monograph 1980-4. *See* also Benston, "The Persistent Myth of Redlining," *Fortune* (March 13, 1978) at 66-69. Yet these reports have themselves been harshly criticized, and have been accused of assuming as a given the proposition they are supposed to be testing. 1988 CRA Hearings, *supra* note 14, at 110. *See*, e.g., Guttentag & Wachter, *supra*, at 4 ("Redlining is a problem mainly because the private risk and cost of lending in redlined areas or to protected groups is excessive.")

    One of the fundamental points of contention among the researchers has to do with the proper measurement of mortgage demand in inner-city neighborhoods. Because mortgage applications data is generally not publicly available, and because other evidence of mortgage demand is difficult to collect, statistical studies often rely on proxies to measure demand. Yet as Allen Fishbein, General Counsel of the Center for Community Change, has noted, the impressive success of many recent affirmative lending programs attests to the fact that a very active demand for credit exists in urban neighborhoods. 1988 CRA Hearings, *supra* note 14, at 449-50. Lenders themselves have admitted that the market for credit in these area is much greater than they had anticipated. *Atlanta Constitution*, May 4, 1988, at 1A. Moreover, the criticisms leveled at earlier redlining studies have, to a large degree, been answered in the more sophisticated recent studies that have used additional available data to control for other possible explanations of poor lending patterns, such as demand and market conditions.

22. The Attorney General's 1986 Annual Report to Congress Pursuant to the Equal Credit Opportunity Act Amendments of 1976, at 6; The Attorney General's 1987 Annual Report to Congress Pursuant to the Equal Credit Opportunity Act Amendments of 1976, at 3.

23. *Id.*

24. Board of Governors of the Federal Reserve System, 73rd Annual Report, 167 (1986); Board of Governors of the Federal Reserve System, 74th Annual Report, 158-59 (1987). Prior to 1986 regulated institutions had shown a steady increase in compliance with the requirements of Regulation B, reaching a high of 81 percent compliance in 1985. Board of Governors of the Federal Reserve System, 67th Annual Report, 177 (1980); Board of Governors of the Federal Reserve System, 68th Annual Report, 154 (1981); Board of Governors of the Federal Reserve System, 69th Annual Report, 155 (1982); Board of Governors of the Federal Reserve System, 70th Annual Report, 160 (1983); Board of Governors of the Federal Reserve System, 71st Annual Report, 153 (1984); Board of Governors of the Federal Reserve System, 72nd Annual Report, 151 (1985).

    The most frequent violations of Regulation B are (a) failing to provide an adequate written notice of adverse action, (b) failing to provide notice of action taken within thirty days of receiving a completed application, (c) illegally requiring the signature of a spouse or cosigner, (d) failing to request information for monitoring purposes, and (e) illegally inquiring about the sex of an applicant.

25. *Compare* Board of Governors' 1983 and 1987 Annual Reports.

26. Letter from Robert L. Clarke, Comptroller of the Currency, to U.S. Rep. Frank Annunzio (undated).

27. Attachment to letter from Jerauld C. Kluckman, Director, Division of Compliance Programs, Federal Home Loan Bank System, to Stephen M. Dane (Aug. 26, 1988). In 1982 the Bank Board received 68 discrimination complaints. In 1987 it received 236. The percentage of these complaints that the Board found meritorious ranged from a low of 3 percent in 1983 to a high of 21 percent in 1982. *Id.*

28. Private mortgage insurers issue mortgage insurance that protects the lender should the borrower default, up to a specified amount (usually 20 percent of the loan amount). They play a significant role in the housing finance industry, for virtually all lenders and many states require private mortgage insurance for loans with less than 20 percent equity invested by the borrower

29. As part of the mortgage loan transaction, the borrower signs a note requiring payment of the borrowed principal and interest to the lender. Like other forms of commercial paper, this note can be bought, sold, assigned, and transferred. Market activity in mortgage notes and related documents is called the secondary mortgage market or secondary market.

30. See 1988 CRA Hearings, *supra* note 15, at 24-27, 39-40, 260, 450; Kantor & Nystuen, "De Facto Redlining A Geographic View," 58 *Economic Geography* 309, 310-11 (1982).

31. *Id.*

32. *See*, e.g., Squires & Velez, "Insurance Redlining and the Transformation of an Urban Metropolis," 23 *Urb. Aff. Q.* 63 (1987); Badain, "Insurance Redlining and the Future of the Urban Core," 16 *Colum. J.L. & Soc. Probs.* 1 (1980); H.R. Rep. No. 865, 96th Cong., 2d Sess. 8 (1980).

33. *See* 1988 CRA Hearings, *supra* note 15, at 7 (statement of Senator Proxmire), 33 (statement of Gale Cincotta), 96 (statement of Calvin Bradford).

34. 42 U.S.C. § 3605. The new Fair Housing Amendments Act of 1988 will substantially revise the wording of § 3605 and will expand its coverage . Except where noted, however, the revisions should not affect the discussion that follows.

35. *See, e.g., Laufman v. Oakley Building & Loan Company*, 408 F. Supp. 489 (S.D. Ohio 1976); *Harrison v. Otto G. Heinzroth Mortgage Company*, 414 F. Supp. 66 (N.D. Ohio 1977). In one recent case, the plaintiffs were white sellers of property for which a mortgage loan application had been made, and the white realtor involved in the transaction. The applicants themselves were not even parties to the suit. *Old West End Association v. Buckeye Federal Savings & Loan*, Fair Housing-Fair Lending (P-H) Para. 15,548 (N.D. Ohio 1986). The plaintiffs there were injured because the lender forced a modification of the sales contract, allegedly based on the racial characteristics of the neighborhood in which the property was located, that required the sellers to reduce their sales price and, therefore, lose money on the transaction. That alleged harm to the sellers was enough, the court held, to assert a claim under the Fair Housing Act.

36. *See* H.R.1158, 100th Cong., 2d Sess., Cong. Rec. H6491-501 (daily ed. Aug. 8, 1988).

37. 42 U.S.C. § 3610(a) (repealed).

38. *Old West End Association v. Buckeye Federal Savings & Loan*, 675 F. Supp. 1100, 1103 (N.D. Ohio 1987) (neighborhood discrimination); *Thomas v. First Federal Savings Bank of Indiana*, 653 F. Supp. 1330, 1338 (N.D. Ind. 1987) (applicant discrimination).

39. *See, e.g., Conference of Federal Savings & Loan Associations v. Stein*, 604 F.2d 1256, 1258 (9th Cir. 1979), aff'd mem., 445 U.S. 921 (1980); *Thomas v. First Federal Savings Bank of Indiana*, 653 F. Supp. 1330, 1337 (N.D. Ind. 1987); *Harrison v. Otto G. Heinzroth Mortgage Co.*, 414 F. Supp. 66 (N.D. Ohio 1976); *Laufman v. Oakley Building & Loan Company*, 408 F. Supp. 489 (S.D. Ohio 1976). *See* also 73 A.L.R. Fed. 899.

40. *See, e.g.*, 12 C.F.R. § 528.2(a), § 528.3, § 531.8.

41. *See Lindsey v. Modern American Mortgage Corp.*, 383 F. Supp. 293 (N.D. Tex. 1973); *Harper v. Union Savings Association*, 429 F. Supp. 1254 (N.D. Ohio 1977).

42. *See, e.g., Love v. DeCarlo Homes, Inc.*, 482 F.2d 613 (5th Cir. 1973), cert. denied, 414 U.S. 1115 (1973); *Clark v. Universal Builders, Inc.*, 501 F.2d 324 (7th Cir.), *cert. denied*, 419 U.S. 1070 (1974), *on remand*, 409 F. Supp. 1274 (N.D. Ill. 1976), 706 F.2d 204 (7th Cir. 1983).

43. *Hanson v. Veterans Administration*, 800 F.2d 1381 (5th Cir. 1986); *United States v. American Institute of Real Estate Appraisers*, 442 F. Supp. 1072 (N.D. Ill. 1977), *appeal dismissed*, 590 F.2d 242 (7th Cir. 1978).

44. *Compare McDiarmid v. Economy Fire & Casualty Co.*, 604 F. Supp. 105 (S.D. Ohio 1984), and *Dunn v. Midwestern Indemnity MidAmerican Fire & Casualty Co.*, 472 F. Supp. 1106 (S.D. Ohio 1979), 88 F.R.D. 191 (S.D. Ohio 1980), with *Mackey v. Nationwide Insurance Companies*, 724 F.2d 419 (4th Cir. 1984).
45. *Evans v. First Federal Savings Bank of Indiana*, 669 F. Supp. 915, 923-24 (N.D. Ind. 1987).
46. 15 U.S.C. § 1691.
47. 15 U.S.C. § 1691(e).
48. *Old West End Association v. Buckeye* Federal Savings & Loan, Fair Housing-Fair Lending (P-H) Par. 15,548 (N.D. Ohio 1986); *Evans v. First Federal Savings Bank of Indiana*, 669 F. Supp. 915 (N.D. Ind. 1987).
49. Gorman, "Enforcement of the Equal Credit Opportunity Act," 37 *Bus. Law.* 1335, 1345-48 (1982); Schellie, "Consumer Financial Services Law: Equal Credit Opportunity," 41 *Bus. Law.* 1029, 1037 (1986).
50. *See, e.g.*, *Cherry v. Amoco Oil Co.*, 490 F. Supp. 1026 (N.D. Ga. 1980). The regulatory agencies have emphasized that mortgage lending policies will be subject to analysis under the "effects test." *See* 12 C.F.R. § 202.6, 12 C.F.R. § 531.8, 12 C.F.R. § 701.31(e).
51. 15 U.S.C. § 1691c(d). The agencies are the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board, the National Credit Union Administration, the Interstate Commerce Commission, the Civil Aeronautics Board, the Secretary of Agriculture, the Farm Credit Administration, the Securities & Exchange Commission, the Small Business Administration, and the Federal Trade Commission.
52. 15 U.S.C. § 1691e.
53. 42 U.S.C. §§ 1981, 1982, 1983.
54. *Evans v. First Federal Saving Bank of Indiana*, 669 F. Supp. 915 (N.D. Ind. 1987); *Contract Buyers League v. F & F Investment*, 300 F. Supp. 210 (N.D. Ill. 1969), aff'd on other grounds, 420 F.2d 1191 (7th Cir.), *cert. denied*, 400 U.S. 821 (1970); *cf. Jones v. Alfred H. Mayer Co.*, 392 U.S. 409, 413 n.10 (1968). One of the most expensive readings of § 1982 established the proposition that housing developers are prohibited by that section from "exploiting" a dual housing market created over the years by other actors in the market. *Clark v. Universal Builders, Inc.*, 501 F.2d 324 (7th Cir.), *cert. denied*, 419 U.S. 1070 (1974), *on remand*, 409 F. Supp. 1274 (N.D. Ill. 1976), 706 F.2d 204 (7th Cir. 1983).
55. The concept of race discrimination embodied in them is broad enough to include one's ethnic background or ancestry. *See St. Francis College v. Al-Khazragi*, 107 S.Ct. 2022 (1987); *Shaare Tefila Congregation v. Cobb*, 107 S.Ct. 2019 (1987).
56. 42 U.S.C. § 2000d.
57. One court has held that Title VI provides a private cause of action for geographic redlining against an institution subject to Federal Home Loan Bank Board regulations. *Laufman v. Oakley Building & Loan Company*, 408 F. Supp. 489 (S.D. Ohio 1976). Another has held, however, that Title VI does not provide a private cause of action to a rejected home repair loan applicant for alleged discrimination under a community development block grant program. *Nabke v. U.S. Department of Housing & Urban Development*, 520 F. Supp. 5 (W.D. Mich. 1981). *See also Allen v. Brodie*, 573 F. Supp. 87 (D. Md. 1983), *appeal dismissed*, 729 F.2d 1451 (1984) (dismissing action alleging discrimination in the implementation of city loan programs).
58. U.S. Commission on Civil Rights, The Federal Fair Housing Enforcement Effort 59 (1979).
59. 42 U.S.C. § 5309.
60. *Id.*
61. *Nabke v. U.S. Department of Housing & Urban Development*, 520 F. Supp. 5 (W.D. Mich. 1981).
62. 12 U.S.C. § 1735f-5(a).

63. A "federally related" mortgage loan is one that is secured by residential property designed for occupancy of from one-to- four families, and (1) is made by a lender whose deposits are insured by a federal agency or by a lender regulated by a federal agency, or (2) is insured, guaranteed, or assisted by HUD or any other agency of the federal government, or (3) is eligible for purchase by the Federal National Mortgage Association (FNMA), the Government National Mortgage Association (GNMA), or the Federal Home Loan Mortgage Corporation (FHLMA), or (4) is made by any "creditor" who makes or invests in residential real estate loans aggregating more than $1,000,000 per year. 12 U.S.C. § 1735f-7(b). The term "creditor" is defined to include a person or organization that regularly extends consumer credit payable in more than four installments and is the person or organization to whom the debt is initially payable. 15 U.S.C. § 1602(f).
64. 12 U.S.C. § 2801.
65. 12 U.S.C. § 2803. The term "depository institution" means commercial banks, savings and loan associations, and credit unions which make " federally related" mortgage loans. 12 U.S.C. § 2802 (2). *See* note 63 *supra*; 12 C.F.R. § 203.2(c). Non-depository institutions, such as mortgage companies that are unaffiliated with depository institutions, are not subject to the Act or any regulations promulgated under it.
66. S. Rep. No. 187, 94th Cong., 1st Sess. 2 (1975).
67. 12 U.S.C. § 2901.
68. *Id.* The Senate believed that existing law provided general authority to the federal financial supervisory agencies to assess a regulated lender's performance in meeting the credit needs of urban communities, but that the regulating agencies were not adequately doing so. S. Rep. No. 175, 95th Cong. 1st Sess. 33 (1977). The Senate Banking Committee criticized the Federal Home Loan Bank Board and other federal financial supervisory agencies for not monitoring lenders' performances in these areas. *Id.* at 33-35. The Committee reemphasized, as it did in promoting the enactment of the Home Mortgage Disclosure Act in 1975, the "amply documented cases of redlining."
69. *See*, *e.g.*, 12 C.F.R. § 543.2.
70. The Comptroller of the Currency has issued regulations implementing CRA (12 C.F.R. Part 25), ECOA and Title VIII (12 C.F.R. Part 27). The Federal Reserve Board has issued Regulation B implementing ECOA (12 C.F.R. Part 202) and Regulation C implementing HMDA (12 C.F.R. Part 203). The FDIC has issued regulations implementing ECOA and Title VIII (12 C.F.R. Part 338), and CRA (12 C.F.R. Part 345). The Federal Home Loan Bank Board has issued regulations implementing Title VIII and ECOA (12 C.F.R. Part 528), Title VI (12 C.F.R. Part 529), CRA (12 C.F.R. Part 563e) and the Federal Home Loan Bank Act (12 C.F.R. Sec. 531.8). The National Credit Union Administration has issued regulations implementing ECOA and Title VIII (12 C.F.R. § 701.31). The Small Business Administration has also issued nondiscrimination regulations implementing ECOA and Title VI (13 C.F.R. Part 113).
71. *See* generally U.S. Commission on Civil Rights, *supra* note 58, at 78, 82-88.
72. 12 C.F.R. Part 202.
73. 12 C.F.R. Part 528; 12 C.F.R. § 531.8.
74. For a more detailed discussion of the relative strengths and weaknesses of all of these regulations, see U.S. Commission on Civil Rights, *supra* note 58, at 82-88.
75. *See*, *e.g.*, U.S. Commission on Civil Rights, *supra* note 58; Citizens' Commission on Civil Rights, *supra* note 1.
76. This is not to suggest that other legislation of the 1980s has not had an indirect impact on equal credit access issues. To the contrary, deregulation of the financial industry and the secondary mortgage market in the early 1980s has had a profound impact on the ability of minorities and low-income applicants to obtain access to credit. *See*, *e.g.*, 1988 CRA Hearings, *supra* note 15, at 96-97, 107-08. An analysis of the indirect consequences of such legislation, however, is beyond the scope of this paper.
77. H.R. 1158, 100th Cong., 2d Sess., Cong. Rec. H6491-501 (daily ed. Aug. 8, 1988).
78. P.L. No. 100-242, 101 Stat. 1815.

79. *See* Art, "Social Responsibility in Bank Credit Decisions: The Community Reinvestment Act One Decade Later," 18 *Pacific L.J.* 1071, 1082 (1987); Potomac Institute, *supra* note 1, at 11; H.Rep. No. 561, 94th Cong., 2d Sess. 20 (1975), *reprinted in* 1975 U.S. Code Cong. & Admin. News, 2303 2321; 1988 CRA Hearings, *supra* note 15, at 85, 450.
80. Citizens' Commission on Civil Rights, *supra* note 1, at 55-56.
81. *Id.* at 70-71.
82. *Id.*
83. *See* Schlay, *supra* note 12, at 141 n.3; 1988 CRA Hearings, *supra* note 15, at 107.
84. Board of Governors of the Federal Reserve System, 72nd Annual Report 147-49 (1985); Schellie, *supra* note 48, at 1029-35.
85. *See* 12 C.F.R. § 202.2(e); 12 C.F.R. § 202.13.
86. Board of Governors of the Federal Reserve System, 72nd Annual Report 147-48 (1985); Board of Governors of the Federal Reserve System, 73rd Annual Report 174-75 (1986); Schellie, *supra* note 49, at 1034-35. A recent legislative proposal by Rep. St. Germain, H.R. 5094, would require the Board to issue regulations requiring recordkeeping and adverse action notices with respect to business and commercial loans. *See* H.R. Rep. No. 822, 100th Cong., 2d Sess. 9 (1988). As of this writing, the bill is before the House Judiciary and Energy and Commerce Committees.
87. 52 Fed. Reg. 10733 (1987).
88. 53 Fed. Reg. 30831 (1988).
89. U.S. Commission on Civil Rights, *supra* note 58, at 90.
90. Ryker, Pol, & Guy, Racial Discrimination as a Determination of Home Improvement Loans, 21 *Urban Studies* 177 (1984).
91. *See* Section III *supra*. *See* also Schellie, *supra* note 49, at 1037.
92. U.S. Commission on Civil Rights, *supra* note 58, at 57-75; Washington Council of Lawyers, Reagan Civil Rights: The First Twenty Months 11-23 (undated); Citizens' Commission on Civil Rights, *supra* note 1, at 72-78.
93. U.S. Commission on Civil Rights, *supra* note 58, at 57-75.
94. *Id.* at 57. Between 1976 and 1982 the Department filed a total of only 12 cases under ECOA. Gorman, Enforcement of the Equal Credit Opportunity Act, 37 *Bus. Law.* 1335, 1345 (1982).
95. The court in that case held that the prohibitions of Title VIII apply to appraisers of real estate and to appraisal practices. *United States v. American Institute of Real Estate Appraisers*, 442 F. Supp. 1072, 1078-79 (1977), *appeal dismissed*, 590 F.2d 242 (7th Cir. 1978).
96. *Laufman v. Oakley Building & Loan Co.*, 408 F. Supp. 489 (S.D. Ohio 1976).
97. *Markham v. Colonial Mortgage Service Co.*, 605 F.2d 566 (D.C. Cir. 1979).
98. *United States v. Beneficial Corporation*, 492 F. Supp. 682 (D.N.J. 1980), *aff'd without opinion*, 673 F.2d 1302 (3d Cir. 1981); *United States v. American Future Systems, Inc.*, Civil Action No. 78-1517 (E.D.Pa., Jan. 29, 1981); *United States v. Great Western Bank & Trust*, Civil Action No. 80-1026-PHX-CLH (D. Ariz. May 13, 1981).
99. *Emigrant Savings Bank v. Elan Mgmt. Corp.* (E.D. N.Y.), discussed in The Attorney General's 1982 Report to Congress Pursuant to the Equal Credit Opportunity Act Amendments of 1976, at 3.
100. *U.S. v. Avco Financial Services*, C.A. No. Y-82-3032 (D. Md.).
101. *See* The Attorney General's 1980 Report to Congress pursuant to the Equal Credit Opportunity Act Amendments of 1976, at 3-6; The Attorney General's 1981 Report to Congress Pursuant to the Equal Credit Opportunity Act Amendments of 1976, at 1-4; The Attorney General's 1982 Report to Congress Pursuant to the Equal Credit Opportunity Act Amendments of 1976, at 2-3; The Attorney General's 1983 Report to Congress Pursuant to The Equal Credit Opportunity Act Amendments of 1976, at 2-3; The Attorney General's 1984 Report to Congress Pursuant to The Equal Credit Opportunity Act Amendments of 1976, at 2-4; The Attorney General's 1985 Report to Congress Pursuant to The Equal Credit Opportunity Act Amendments of 1976, at 1-5; The Attorney General's 1986 Report to Congress Pursuant to The Equal Credit Opportunity Act Amendments of 1976, at 1-3; The Attorney General's 1987 Report to Congress Pursuant to The Equal Credit Opportunity Act Amendments of 1976, at 1-5; The Attorney General's 1988 Report to Congress Pursuant to the Equal Credit Opportunity Act Amendments of 1976, at 1-3.

102. *Id.*

103. The decrees typically require affirmative action, such as the establishment of educational or training programs, recordkeeping and reporting, and relief for identifiable victims of the lender's discriminatory policies. *Id. See* also Gorman, *supra* note 94, at 1343.

The Department did conduct one trial in an equal credit case during the 1982 fiscal year. *United States v. American Future Systems, Inc.*, C.A. 78-1517 (E.D. Pa.). The case was filed four years earlier, in 1978. This is the only equal credit opportunity case the Department of Justice has ever litigated through trial.

104. *United States v. ITT Consumer Financial Corp.*, 816 F.2d 487 (9th Cir. 1987).

105. *See* Attorney General ECOA Reports, *supra* note 101.

106. *United States v. Landmark Financial Services*, 612 F. Supp. 623 (D. Md. 1985).

107. U.S. Commission on Civil Rights, *supra* note 58, at 57, 63-64. *But see* Gorman, *supra* note 94, at 1341 (suggesting that despite its lack of subpoena power, most creditors assist in the fact gathering process).

108. In 1982, for example, the Department rejected the use of statistical studies as "not an effective method" of enforcing the law, despite the U.S. Civil Rights Commission's strong recommendation in 1979 to do so. The Attorney General's 1983 Report to Congress Pursuant to The Equal Credit Opportunity Act Amendments of 1976, at 4. *See* U.S. Commission on Civil Rights, *supra* note 58, at 64-66.

109. Barefoot, Gorman, & Geary, "Enforcement and Litigation Under the Equal Credit Opportunity Act," 37 *Bus. Law*. 1351, 1353 (1982).

110. *See, e.g.*, Attorney General 1980 and 1981 ECOA Reports, *supra* note 101.

111. Attorney General ECOA Reports, *supra* note 101.

112. U.S. Commission on Civil Rights, *supra* note 58, at 61 n.29.

113. The Attorney General's 1980 Report to Congress Pursuant to the Equal Credit Opportunity Act Amendments of 1976, at 1.

114. *Id.*

115. The Attorney General's 1984 Report to Congress Pursuant to The Equal Credit Opportunity Act Amendments of 1976, at 1.

116. *Id.*

117. *Id.* Compare this to the staff of 17 attorneys and 17 paralegal and clerical employees assigned to the old Housing and Credit Section in 1977, which had no responsibilities in these other areas. U.S. Commission on Civil Rights, *supra* note 58, at 60.

118. Letter from Paul F. Hancock, Chief, Housing and Civil Enforcement Section, to Stephen M. Dane (August 22, 1988).

119. *Id.*

120. Washington Council of Lawyers, *supra* note 92, at 1-6, 17-23.

121. *Id.* at 19-22.

122. *See* discussion *infra*.

123. *See* discussion in Section II *supra*.

124. 42 U.S.C. § 3610(a).

125. 42 U.S.C. § 3610(c).

126. Letter from Burton Bloomberg, Associate General Counsel for Administrative and General Law, U.S. Department of Housing and Urban Development, to Stephen M. Dane (July 22, 1988).

127. *See* Citizens' Commission on Civil Rights, *supra* note 1, at 41.

128. 12 C.F.R. Part 202.

129. 12 C.F.R. Part 528; 12 C.F.R. § 531.8.

130. 15 U.S.C. § 1691c(a).

131. 12 U.S.C. § 2804(b).

132. 12 U.S.C. § 2902.

133. The following discussion excludes any analysis of the enforcement efforts of the National Credit Union Administration, which has no enforcement responsibility under CRA.

134. Art, *supra* note 79, at 1105-07. The Senate Committee on Banking, Housing, and Urban Affairs felt that existing law provided sufficient authority for the federal agencies to encourage lenders to meet the credit needs of their primary service areas, but that new legislation was necessary because the regulatory agencies "lack[ed] systematic, affirmative programs" to achieve that result. S. Rep. No. 175, 95th Cong., lst Sess. 33-35 (1977). The Senate Committee had earlier noted that the Federal Home Loan Bank Board regulation prohibiting redlining had no practical effect because there existed no meaningful enforcement policy. S. Rep. No. 187, 94th Cong., lst Sess. 10 (1975). *See* also Comment, *supra* note 1, at 146-50.

135. S. Rep. No. 175, 95th Cong., 1st Sess. 33 (1977).

136. Art, *supra* note 79, at 1106. *See* also *id.* at 1123 and n.218.

137. Mortimer, Current Developments in CRA Enforcement, 98 Bank. L. J. 604, 609 (1981); Art, *supra* note 79, at 1119.

138. Art, *supra* note 79, at 1115.

139. *See*, *e.g.*, 12 C.F.R. § 543.2(e).

140. Art, *supra* note 79, at 1095-1101.

141. *Id.* at 1108.

142. *See* generally 1988 CRA Hearings, *supra* note 15.

143. Each financial institution is rated on a scale of 1 to 5, with a 5 representing the lowest level of performance. Level 1 means the institution has a strong record of meeting community needs. Level 2 means the institution has an acceptable record of meeting community credit needs, although some encouragement to improve may be warranted. Levels 3 and 4 mean less than satisfactory and unsatisfactory performance, respectively. Level 5 means the institution's record is substantially inadequate. *See* Federal Reserve System Compliance Handbook, at II.1.55 (1982).

144. *For example*, despite the increasing evidence of a lack of commitment by financial institutions to provide for the credit needs of minority and urban communities, 97 percent of all regulated lenders were given high or satisfactory ratings by the banking agencies. 1988 CRA Hearings, *supra* note 15, at 7. In 1986 nearly 99 percent of the banks examined received passing CRA ratings, *id.* at 271, and in 1985 almost 99 percent of all thrifts examined received favorable ratings. *Id.* at 158. As early as 1983 the Federal Reserve Board's Consumer Advisory Council criticized the rating system. Unfortunately, the Board did not implement the Council's recommendations. *Id.* at 101, 158.

145. *Id.* at 20-22, 101-07, 154-57. All of the agencies have, since 1980, reduced the amount of resources dedicated to examining lender compliance with the community reinvestment statutes and regulations. According to Bank Watch, the combined manhours dedicated to consumer examinations by the Comptroller, the FDIC, and the Federal Home Loan Bank Board fell from approximately 808,335 in 1981 to only 209,881 in 1984, a decline of 74 percent. 1988 CRA Hearings, *supra* note 15, at 155. In 1982 the Comptroller abandoned a vigorous consumer compliance examination program in part "to contribute to [the Reagan] administration effort to reduce regulatory burdens in the market place." *Id.* at 250-51. While the Federal Reserve Board examined 894 of its 1,011 member state banks in 1980, in 1986 the Board conducted only 576 CRA reviews. Board of Governors of the Federal Reserve System, 74th Annual Report, at 162 (1987). Although the FDIC supervises nearly 9,000 banks, it has been able to conduct examinations of only approximately 20 percent of those banks each year, even in high examination volume years. *Id.* at 228, 230. *See* also Art, *supra* note 79, at 1108-09. The Federal Home Loan Bank Board and the FDIC admit that the crisis in the financial industry in the early 1980's has forced them to devote a substantial amount of their resources to safety and soundness concerns to the exclusion of CRA and other consumer-related issues. 1988 CRA Hearings, *supra* note 15, at 228, 266. The Comptroller acknowledges that its replacement examination program was "impaired" by an increase in bank failures and in the number of banks requiring special supervision. *Id.* *See* also Art, *supra* note 79, at 1111-12.

146. 1988 CRA Hearings, *supra* note 15, at 102-107, 160-63. In the entire decade after CRA was passed, only eight out of 40,000 applications for regulatory approval were denied by the agencies. *Id.* at 7. Between 1978 and 1987 the Federal Reserve Board received over 14,000 applications, 112 of which were CRA protested. *Id.* at 216. Despite the large volume of applications and protests, the board never denied an application only on CRA grounds. Since enactment of the CRA in 1977, the Comptroller's office has denied only 4 applications due to CRA factors. *Id.* at

251. None have been denied since 1981. *Id.* at 257. Since the CRA was passed the Federal Home Loan Bank Board has denied only one application on CRA grounds. *Id.* at 269. The Bank Board has routinely approved--sometimes with conditions, sometimes not-- applications from institutions with unsatisfactory CRA ratings. *Id.* at 271. The FDIC has denied only three applications due to CRA factors. *Id.* at 226. This accounts for .01 percent of the total number of applications the FDIC received that were subject to the CRA. *Id.* at 160-63, 226.

147. *Id.* at 255. The Comptroller is also credited with suggesting that competition, not regulation, will force banks to meet their community reinvestment obligations. *Id.* at 14.

148. *Id.* at 231. *See* also Art, *supra* note 79, at 1122.

149. Art, *supra* note 79, at 1139.

150. "Using Banks to Rebuild Neighborhoods," *Philadelphia Enquirer*, July 20, 1987; "Protests Haven't Stopped Bank Mergers," *American Banker*, Oct. 8, 1987; 1988 CRA Hearings, *supra* note 15, at 7. Between the time CRA was passed and 1985 more than 100 community reinvestment agreements had been struck. "Ten Years After Passage of the Community Reinvestment Act--A Resurgence of Interest?," *Perspectives* 10 (Summer/Fall 1986). For discussions of specific examples of community reinvestment agreements negotiated in response to CRA protests or threatened protests, see Weiss & Metzger, Neighborhood Lending Agreements: Negotiating and Financing Community Development, Lincoln Institute of Land Policy, Occasional Paper Series No. 88-06 (March 1988); Schellie, Current Developments With the Community Reinvestment Act, 42 *Bus. Law.* 943 (1987).

151. Art, *supra* note 79, at 1139; Comment, "Redlining Disinvestment and the Role of Mutual Savings Banks: A Survey of Solutions," 9 *Fordham Urban L.J.* 89, 116-17 (1980).

152. *See* Board of Governors of the Federal Reserve System, 67th Annual Report 177 (1980); Board of Governors of the Federal Reserve System, 68th Annual Report 154 (1981); Board of Governors of the Federal Reserve System, 69th Annual Report 156 (1982); Board of Governors of the Federal Reserve System, 70th Annual Report 160-61 (1983); Board of Governors of the Federal Reserve System, 71st Annual Report 153 (1984); Board of Governors of the Federal Reserve System, 72nd Annual Report 151 (1985); Board of Governors of the Federal Reserve System, 73rd Annual Report 167 (1986); Board of Governors of the Federal Reserve System, 74th Annual Report 159 (1987).

153. Schellie, *supra* note 49, at 1035-36. The FTC's leadership role in enforcement of ECOA is part of the statutory scheme. Section 704 of the Act places overall enforcement authority in the hands of the FTC, at least for those creditors that are not subject to regulatory oversight by one of the regulatory agencies listed in the Act. *See* 15 U.S.C. § 1691c. In addition, the FTC has broad administrative and enforcement powers other agencies lack. It can, for example, bring a lawsuit in its own name against a discriminating creditor. *See* 15 U.S.C. § 45 (M) (1) (A), § 57b. Finally, its interests are not as intertwined with the creditors it regulates as are the interests of other federal supervisory agencies.

154. *See* authorities cited in note 152 *supra*.

155. *Id.*

156. Board of Governors of the Federal Reserve System, 71st Annual Report 153 (1984).

157. *See, e.g.*, Board of Governors of the Federal Reserve System, 72nd Annual Report 151-52 (1985). It should be noted that the Federal Reserve Board has also endorsed the use of testing in determining whether a creditor is violating ECOA. Board of Governors of the Federal Reserve System, 71st Annual Report 150 (1984). It apparently does so, however, only after an examination has revealed possible illegal discrimination.

158. Two Federal Home Loan Bank Board regulations address the issue, but only sparingly. 12 C.F.R. § 528.4 prohibits any lender who is a member of a federal home loan bank from directly or indirectly engaging in any form of advertising which implies or suggests a policy of discrimination or exclusion in violation of the Fair Housing Act or the Equal Credit Opportunity Act. 12 C.F.R. § 531.8(d) cautions against the use of advertising or marketing practices that improperly restrict a lender's clientele to only certain segments of the community.

159. *See* Ga. Code Ann. § 8-3-202 (14) (1978); Ky. Rev. Stat. Ann. § 344.367 (1980); Ohio Rev. Code § 4112.02 (H) (4) (1988); Tenn. Code Ann. § 4-21-601 (A) (7) (B) (1984); Wis. Stat. Ann. § 101.22 (2) (1971).

160. Board of Governors of the Federal Reserve System, 72nd Annual Report 156-57 (1985).

Senator DIXON. Thank you very much, Mr. Dane.

And, last, but certainly not least, Ms. Shanna L. Smith, representing the National Fair Housing Alliance and the Toledo Fair Housing Center.

SHANNA L. SMITH, REPRESENTING THE NATIONAL FAIR HOUSING ALLIANCE AND THE TOLEDO FAIR HOUSING CENTER, TOLEDO, OH

Ms. SMITH. Thank you.

My name is Shanna Smith, and the Alliance asked me to represent them because Toledo has been involved in the most cases of litigation under mortgage lending discrimination in the country, and because during the past 3 years alone, we have received over a hundred complaints of lending discrimination.

And out of those complaints, last year, we received 42 complaints, and 13 or 38 percent of those indicated discrimination that was successfully resolved. Eight are still pending, a HUD investigation or litigation in Federal District Court.

And I find it incredible, as you do, that the Federal regulators have complaints and they find no instances of discrimination.

It's extremely troubling to me when I read that the FDIC had 711 fair housing complaints and they found not one single instance of discrimination.

And HUD's comment that they had only received six complaints, you know, I'm sure that's accurate because the private fair housing groups—there are about 50 of us across the country, and States which have absolutely none.

In fact, Illinois, Michigan, Ohio and California have the most private fair housing centers. Mississippi, Arkansas, Louisiana, Alabama have no private fair housing centers. Atlanta is the only one in Georgia. One is just starting in Florida. And there's a small one in Memphis, Tennessee.

There are States throughout this country where victims of housing discrimination receive no assistance because there are no private fair housing centers and state civil rights agencies are largely unresponsive to housing discrimination complaints.

As a result, HUD has so few complaints because right now, they are really being overwhelmed with the cases of familial status and handicapped under the new legislation. And they're adjusting to the new process that they're involved in.

But, also, those of us in the private fair housing field know that HUD does not yet have the capability to investigate the complex issue of lending discrimination complaints, although the Toledo center has submitted several cases to HUD. Most of our cases are either negotiated with the lender or we go directly into Federal district court.

The problem with underreporting in the country, as the Federal Reserve person talked about, is that people may not recognize discrimination is occurring. And then, when you'd walk into a bank and if you're denied a loan, you have to deal with the comments that the loan officer makes to you.

For example, I know in my own case when we purchased our home in a well-integrated neighborhood, they reduced the terms and condition for years by saying our house didn't have good economic life.

I really didn't know what that meant. And we have other cases where the loan officer said, "Well, the appraisal shows that the house is functionally obsolete."

And we ask, "What does that mean?"

In one instance, we met with the lender and the appraiser regarding an historic older home in a neighborhood that's 51 percent black. The appraiser alleged that the walk-in closets were "functionally obsolete."

And we scratched our heads and said, "But, in the newer homes, you have a whole wall that is a closet filled with doors that slide across the whole wall."

What is more functional? A door where you can walk in and put a headboard and a dresser and a bed and use the rest of the wall, or that?

The lender granted that particular loan.

What we found——

Senator DIXON. This worries me a little. I live in a 94-year-old house on the hill. [Laughter.]

Ms. SMITH. You should be worried because what we find, as Mr. Dane talked about, is that some policies arbitrarily exclude older neighborhoods which can translate to minority and integrated neighborhoods.

And my colleagues from Detroit should be very proud of the billion dollars plus that they have going into their neighborhoods.

But, in Toledo, what we found is that, when we have that commitment made by the lenders, we still have to challenge the policies that they have in place that prohibit that money from being expended.

For example, when the appraisers come in, if you have—well, many appraisers have policies that discriminate against older neighborhoods. The terms that they may use, such as "predominant value." A case that comes to mind that was filed in Federal district court and successfully settled out-of-court in Toledo involved "predominant value."

The property appraised out properly. But, on the back of the appraisal, it had a section called Predominant Value. And the lender said: "We wouldn't lend more than $70,000 on any home in this neighborhood." It was a mixed neighborhood racially and by the style and price of housing. Homes in the neighborhood sold for $30,000 up to $200,000.

In that instance, the sellers, the real estate agent and the neighborhood sued the savings and loan association, alleging that using this particular policy had a discriminatory impact on the neighborhood.

In a precedent-setting decision by the court in a pretrial motion, the Judge said:

"If an applicant is creditworthy, the home is in a minority area, and the house appraises properly, then the burden to show a nondiscriminatory reason falls upon that lender."

So the court has said to us that if we have clients who are creditworthy and the property appraises properly, there's no reason for them not to secure a mortgage loan.

It seemed very simple to us, but we were very glad when the Federal court pointed that out.

The issue of testing has come up. And, frankly, it frightens me to think that the regulators would do that kind of testing because if they can't find discrimination when they receive hundreds of complaints, I question how they'll be able to structure testing that would uncover discriminatory practices.

We acknowledge in the private fair housing field that this is the most complicated test to do. We are capable of doing it if we have the funds to do it. The difficulty in this testing is finding a creditworthy volunteer tester, finding people who will let us use their homes for sale, and executing agreements between the tester and the home seller so that the house won't actually be sold.

But our greatest difficulty is coming up with the amount of downpayment to put in their account for a 6-month period so that when the lender reviews their application, they will have had that downpayment in that account.

The Private Fair Housing Centers are capable of doing this. When HUD has conducted testing, they have subcontracted with the Private Fair Housing groups. In 1978 and in 1989, to conduct their sales and rental testing, because that is our area of expertise.

In the lawsuits that have come through the Toledo Fair Housing Center, which exceed 10, we haven't had to do testing. During discovery, we have uncovered discriminatory policies and practices.

This minimum loan amount that Allen talked about is significant. In Toledo, that has a disparate impact on 78 percent of the black community and 72 percent of the Hispanic community. Last week, we settled a case, the first case against a private mortgage insurance company, who also had a minimum insurance policy, where they would not write insurance, PMI coverage, for properties under $30,000.

These types of policies that the federal regulators believe their examiners can look at, they've seen these policies for years. They have not recognized that these have a discriminatory impact on women and minorities. So I have little confidence that the federal regulators can monitor themselves.

And one of them actually suggested that the trade industry do the testing. And I can't see member groups policing themselves on those issues.

One thing we would like to recommend is that HUD create, recreate its systemic complaint investigation unit. As Allen has talked about, we feel that the responsibilities for investigation should come under one unit of government. And we would like to see that come under the U.S. Department of Housing and Urban Development. But we would like to see within that unit, not only the fair housing specialists, but people who also have a financial background and a lending/insuring training program for employees in this unit.

When we began our lending investigations, we had staff go through seminars with the financial regulatory people in Toledo and out of the Cleveland Federal Reserve Bank to teach us about lending issues, the appraisal process, and the insuring process so that when we investigate these kinds of complaints, we know what we're looking for and then apply the Fair Housing element to it.

Thank you.

[The complete prepared statement of Shanna L. Smith follows:]

TESTIMONY OF SHANNA L. SMITH
REPRESENTATIVE OF THE
NATIONAL FAIR HOUSING ALLIANCE, INC.
BEFORE THE SENATE SUBCOMMITTEE ON
CONSUMER AND REGULATORY AFFAIRS

I. INTRODUCTION

Members of the Committee, my name is Shanna Smith. I am representing the National Fair Housing Alliance located in Washington D.C. The National Fair Housing Alliance is a non-profit corporation representing more than 50 private fair housing centers throughout the country. NFHA was organized to advance "the policy of the United States to provide . . . for fair housing throughout the United States". We attempt to fulfill this purpose by conducting research into the nature, extent and effects of housing discrimination and by advocating for effective programs of fair housing enforcement and compliance. The NFHA attempts to identify and eliminate housing practices that are discriminatory and that constitute barriers to equal access to housing, including discriminatory lending practices.

I have been asked to represent NFHA because over the past ten years the Toledo Fair Housing Center has received and investigated a large number of lending discrimination complaints. The first racial redlining case in the nation was filed and successfully litigated in Toledo in 1975. (Harrison v. Otto G. Heinzeroth Mortgage Co.) Our office has been instrumental in the investigation and prosecution of at least seven major cases filed in federal district court against lenders doing business in the Toledo area. During the past three years the Center received more than 100 complaints of mortgage lending discrimination.

I would like to cover three issues during my allotted time:

1. Underreporting of discriminatory lending practices;
2. Enforcement: the burden of testing lending complaints; and
3. Recommendations for better enforcement.

UNTOLD STORY --- LENDING DISCRIMINATION IN DISGUISE

I do not believe that anyone has an accurate indication of the amount of mortgage lending discrimination going on in the United States. However, the Toledo Fair Housing Center has received more lending complaints than any other fair housing center and we can give this committee some indication as to the nature and extent of these practices.

The Toledo Fair Housing Center received 979 complaints of housing discrimination during the past three fiscal years. Of these complaints 102 alleged discriminatory lending practices.

"Why Toledo?"

The primary reason Toledo receives so many more complaints is because we made lending issues a priority after the real estate agents told us they wanted to sell properties in the inner-city and integrated neighborhoods, but they ran into so many lending and insuring problems that it wasn't worth the effort.

The Center sought and secured two grants from the Needmor Foundation to specifically investigate, test and litigate mortgage lending and private mortgage insurance complaints. This grant money was matched with Community Development Block Grant funds to hire a research coordinator and researcher/fair housing specialist to tackle the complex problem of mortgage lending discrimination.

First, we conducted a series of television programs and advertising campaigns in the minority press to educate potential victims on how to recognize practices that could constitute a violation of federal or state fair housing laws.

A typical advertisement would read:

> WE DON'T LOAN IN COLORED NEIGHBORHOODS
>
> You won't hear language like that when you are denied a mortgage loan or home equity loan. What you might hear is:
>
> "Your property didn't appraise out."
> "Your income-to-debt ratio is too high"
> "We don't make loans under $30,000"
> "We can't give you a 30-year loan on that property"
> "You need more money for a downpayment, no PMI will insure this home"
>
> These statements MIGHT indicate that you are a victim of mortgage lending discrimination. If you are turned down for a home loan for any reason or if the lender changes the terms or conditions of your loan contact the FAIR HOUSING CENTER.

We also directed our educational outreach to real estate agents and taught them how to spot loan denials or changes in terms and conditions which could violate the fair housing act. As a matter of fact, five of the seven major lawsuits filed were referred to the Center by real estate agents who thought that lending discrimination was occurring.

Approximatley 45% of all housing discrimination complaints show probable cause after an investigation. In 1988-89, the Center received 42 lending complaints. Of these complaints 38% or 13 complaints showed probable cause and were successfully resolved. Eight complaints are still pending litigation or HUD investigation as of July 1, 1989.

I would like to highlight three lending cases that were filed in federal district court and settled after the discovery phase of the litigation.

In the McMillian v Huntington National Bank case, the black couple charged they were denied the loan because of the racial composition of their neighborhood and their race. The McMillians were making $47,000 per year and seeking a ten year mortgage loan of approximately $16,000 on a home that appraised for $26,000. They had been living in this ten year old home of brick and aluminum siding since its construction.

They were buying this home under HUD's Turnkey III Homeownership Program which was a lease with an option to buy program.

The McMillian's adverse action notice stated the only reason for the loan denial was that the "property lacks marketability". There was a willing buyer who was credityworthy, a 10-year old home, an appraisal that placed the value of the home at $10,000 higher than the mortgage request, and a neighborhood that was 96% black. We could not determine any legitimate business reason to refuse this loan application. We concluded that the race of the buyers and the racial composition of the neighborhood influenced the decision to deny this loan application.

The Center later discovered that this same lender had a policy of tiering interest rates for properties under $30,000. The rate would increase by one-half percent in increments of $5,000 until they refused to make any mortgage loan for less than $10,000. In Toledo this policy has a disparate impact on 78% of the black homeowners and 72% of the Hispanic homeowners whose homes are valued at less than $30,000.

This policy and several others identified by the Center as discriminatory were dropped as part of an agreement to not protest this lenders application for a merger and acquistion of other financial institutions.

In the Ramsey v. State Savings Bank, an interracial couple received an adverse action notice stating that they were denied a loan because the property had "inadequate collarteral", the length of time of the wife's employment was too short, and they had an insufficient downpayment.

The property appraised properly, the wife was only 21 years old and had been continuously employed in her line of work for three years, but had recently taken a new job because it offered a promotion and increase in pay. They were seeking a 90/10 loan commitment.

This couple went to local lender and received laon approval without a hitch. The Center reviewed the couple's credit record and found that they paid up to three months in advance on their car loan and fell easiliy within the income-to-debt guidelines.

We concluded that the husband's race and the location of the property in an integrated neighborhood were the real reasons for this loan denial. This case was successfully resolved when the couple received a monetary settlement.

The third suit involves a neighborhood that is 51% black, white uyers, white sellers and a white real estate agent. In the Old West End v. Buckeye Federal Savings and Loan Association case, the terms and conditions for securing a mortgage were changed. The buyers sought a 95/5 loan on a property selling for $78,500. The lender denied the loan stating that the predominant value of homes in the neighborhood was $70,000; therefore, they would not loan more than $70,000 on any property in the Old West End. The sellers were leaving Toledo and decided to reduce the sales price of their home do the loan would be approved. This had effect of reducing the agents commission and artificially reducing property values for at least a 6-month period during which this property could be used as a comparable for other sales in the neighborhood.

In a pre-trial motion the district court decided what constitutes a prima facie case of mortgage lending discrimination from the facts presented in this complaint. In sum, the court said that if the buyer is creditworthy and the house appraises properly, then the burden to show a non-discriminatory reason for the loan denial falls upon the shoulders of the lending insitution. This complaint was settled for an undisclosed amount of money and a policy change shortly after this court decision.

I should add that during discovery in this complaint we found five instances where the mortgage loan requests by whites applying for 95/5 loans for homes in white neighborhoods exceeded the predominant value as shown on the appraisal report, but the loans were granted anyway. We also found three instances where black buyers in black neighborhoods were turned down because the mortgage amount exceeded the predominant value.

DISCRIMINATORY PRACTICES

There are several reasons for the underreporting of lending problems. The first is that being turned down for a mortgage loan is a pretty embarassing experience, especially when the adverse action notice speaks to credit or income-to-debt ratios. As a result, people do not want to discuss a loan denial. There is also a lack of confidence in the systems that are suppose to help rectify acts of discrimination. We are unaware of any state civil rights commission capable of investigating a mortgage lending complaint. Most state commissions handle few housing discrimination complaints and their remedies are fequently very inferior to those secured through private litigation.

Discrimination occurs during one or more of the following steps of the application process.

"Pre-screening"

Discrimination by pre-screening goes pretty much undetected unless a local fair housing group is doing telephone or appointment type testing. Most applicants do not know that when the lender suggests that bank "ABC" has a better interest rate available and they should try that bank first or when the bank offers to "informally qualify" the caller to save them time and money that that behavior can be a form of lending discrimination. Pre-screening is that friendly, smiling face of the 1980's style of denial.

"Application Process"

Most of the problems identified in the applicationprocess involve credit or employment issues.

Our investigations have uncover instances where income from all sources has not being counted. For example, child support and Aid to Dependent Children (ADC) payments have been eliminated from consideration. Also, minorities who work out of unions are required to get income verifications from each employer during the year instead of the lender relying on the applicants income tax statements or verification from the local union hall. We have found cases where the income of spouses, who have consistent parttime employment, is totally disregarded. We even had a case where the lender wrote a letter stating that when the husband became employed again, then the lender would consider the couples' application for the home loan; in spite of the fact that the wife's income alone as a school teacher was sufficient to carry the loan.

Credit problems are frequently cited as the reason for loan denial, but little explanation is given to the applicant on how to verify if the credit information is correct or what it would take to become creditworthy for this lender. There appears to be an unwillingness onthe part of loan officers to gprovide the same credit type counsellig to minority applicants as is given to white applicants.

"Appraisal Process"

Some loan officers make the appraiser the convenient scapegoat for a loan denial by saying "the property did not appraise out and I cannot share the appraisal report with you." Even though the applicant paid for the report, most lenders will not share it. In Toledo, we have negotiated agreements with several lenders to share the report with us, when the appraisal is the basis for the denial.

Explanations from loan officers concerning the appraisal can be very confusing because they use "appraisal" language. What does "economically or functionally obsolete" mean to the average person?

We have studied appraisal books and conducted training for appraisers, but we have yet to learn the formula for computing "predominant value", but lenders rely on this information when approving or denying loan applications.

Older neighborhoods often have a wide variety of housing styles with large differences in pricing. To use predominant value as a measure of the maximum mortgage amount available through a lender can have a disparate impact on minority and ethnic communities.

"Private Mortgage Insurance"

Lenders commonly say the reason for the denial of loans where the downpayment is less than 20% is that they cannot secure PMI coverage. Although it seems that this excuse is used most frequently where the applicants' property is located in an integrated or minority neighborhood.

Lenders will earnestly state that they would make this loan, but they can't get PMI coverage. An easy way to deny a minority loan application that has less than a 20% downpayment is to send it to a PMI company who you know will have a problem with the applicants income source, credit, age or location of housing, or the amount of the loan. Some lenders keep sending an application to different PMI companies until they get coverage. Other lenders stop after the first rejection and then reject the loan altogether.

The recently settled suit Briceno v United Guaranty Residential Insurance Company should eliminate the excuse of the amount of the mortgage loan as a reason for denial. The Toledo Fair Housing Center joined the Hispanic buyers and white sellers in challenging minimum loan amounts for granting PMI coverage.

Two years ago a group ofmortgage lenders from the Canton/Arkon, Ohio area told the Toledo Fair Housing Center that PMI companies were a major obstacle in their ability to meet the credit needs in the minority community. The Center began investigating PMI complaints and the Briceno litigation was a result of our effort to address this obstacle.

"Loan Committee"

Now if the applicant can make it through prescreening, complete an application and become creditworthy, have a home that appraises properly and secure PMI coverage; they still must make it past the loan committee.

If a lender wants to deny the application because of the race or sex of the buyers or the location of the property, this is their last chance. Applicants receive letters stating that the lender can approve the loan if the buyer will shorten the term of the loan or put more money down.

This request can effectively force the applicant to eject the loan commitment. Many times a first time homebuyer has pulled together every penny to cover the downpayment and closing costs and they have no other source of funds to increase their downpayment. Reducing the term of the loan increases the monthly payment and can effectively put the family above the income-to-debt ratio used by the lender.

"Advertising Practices"

To conclude this section on identifying discriminatory lending practices, one must return to the stage of initial contact with potential buyers -- the lender's marketing efforts. Using the equal opportunity slogan alone is not sufficient to attract minority purchasers. A lender must have advertising directed towards the minority and female purchasers, but sadly most advertisements still show a white loan officier talking with a white couple about financing a home. We also routinely find a white male being the spokesperson for a lender. Lenders defend this practice by stating that this person has a trademark voice or appearance and they have spent years developing this image in the community and they are unwilling to change it.

It is important that advertising make people of all racial backgrounds feel welcomed. Advertising that shows a preference or limitation can be a violation of the federal Fair Housing Act. It is our opinion that advertising which relies upon the use of white models exclusively or predominantly acts to discourage minority applicants.

II. TESTING LENDING DISCRIMINATION COMPLAINTS

The second area I want to discuss is the testing of lending discrimination complaints.

The private fair housing centers agree that lending testing is by far the most difficult test to conduct. There are several steps in the loan application process where discrimination can occur; therefore, we must devise testing to cover each step in this process.

Testing for pre-screening is relatively simple. However, to fully evaluate the nature and extent of lending discrimination a tester needs to complete the process from application through loan commitment or denial.

To tackle this, the testing agency must have creditworthy testers and funds to cover the application fee and downpayment. In addition, there must be a home available so an appraisal can be conducted, a purchase offer to present to the lender and sometimes even a cooperating real estate company. The tester and homeowner must execute a release to prevent the sale of the property and everyone involved should be paid for their time and services.

Home equity loan testing is a little less complicated, but still requires a creditworthy cooperating homeowner, a tester and application fee.

In both mortgage lending and home equity testing we may also need funds for an independent appraisal report, if the appraisal becomes a factor in the loan denial or changes in the terms or conditions for loan approval.

We became quite concerned when we learned that HUD, the federal regulators and the industry trade groups would consider conducting testing programs of financial institutions.

First of all HUD has not yet developed the expertise to investigate a lending discrimination complaint. I believe after meeting with the Deputy Assistant Secretary for Fair Housing and Equal Opportunity and Gordon Mansfield, the Special Advisor to Secretary Kemp, that HUD is committed to understanding the complex nature of issues involving lending and insuring practices. At the present time, however, HUD is overwhelmed with housing discrimination complaints in the area of rental and sales practices and has not devoted any special resources to training its staff on lending issues.

HUD has been given the primary responsibility for enforcing the newly amended Fair Housing Act along with the Department of Justice. HUD is playing catch-up in hiring and training staff after the severe reduction in personnel under the Reagan administration.

Historically, HUD has contracted with the private fair housing centers to test the levels of discriminatory housing practice in the sales and rental areas. HUD has no testing experience. HUD relied upon the private fair housing centers across the country to cond ct the Housing Marketing Surbeys in 1978 and 1989.

HUD just does not have the staff or expertise to handle such a complex issues as lending and insurance testing.

The federal regulators may not be a good resource to conduct lending testing either. Although bank examiners are trained to identify financial decisions which affect the safety and soundness of lending decisions, we are not confident that they have the fair housing expertise to identify polcies which have a discriminatory impact or the skills to conduct testing. For example, why have minimum loan amount policies been allowed to exist when it is clear these policies have a disparate impact on minority neighborhoods and female buyers?

I have several questions about te FDIC not finding one instance of discrimination after receiving 711 fair housing complaints by telephone. Who took those calls? What fair housing training did he/she have? Were actual documents reveiwed or was the caller simply questioned? Was an investigation conducted and by whom?

It is our opinion on questions of fair housing that a caller should be provided with the opportunity to speak to someone at HUD or an attorney at the Department of Justice.

Lastly, we do not think it is wise to ask the industry trade associations to test their own members. Self-policing rarely works and the potential for a conflict of interest should be obvious.

Testing requires people who are experts in civil rights and who have a working understanding of the way financial institutions operate.

We believe that a cooperative effort between private fair housing groups and the government regulators and enforcers would be the most useful means to identify the nature and extent of discriminatory lending practices.

NFHA conducted a 2-day national conference in June entitled "Meeting the Challenge - Enforcing the New Fair Housing Act". One whole day was spent on CRA and testing and litigating lending complaints.

NFHA has in place through its membership a network capable of conducting testing in major cities through the United States. If the government is serious about identifying lending problems, then NFHA is willing to cooperate in such an effort.

III. RECOMMENDATIONS

The following are some ideas for better enforcement mechanisms as well as preventive measures to reduce and eliminate mortgage lending discrimination.

1. Create a special Systemic Complaint Investigation Unit within the HUD central office to do two things:

a. Receive and investigate lending and insurance complaints. Lending complaints would include, but not be limited to mortgage loans, homeimprovement loans, home equity loans, and complaints involving the secondary mortgage market. Insurance complaints would include, but not be limited to, private mortgage insurnace companies as well as homeowner and renters insurance companies.

b. Commission studies to determine the nature and extent of discriminatory lending and insuring practices.

2. Establish more resources for receiving and investigating housing discrimination complaints. The Community Development Block Grant program requires recipients (cities) to develop programs to "affirmatively further fair housing". HUD should strongly encourage these cities to fund private fair housing groups to achieve the mandate to affirmative further fair housing. This would result in local monitoring of lending institutions on a very cost effective basis. It would also provide the federal regulators with credible local resources for information about lending policies and practices. The most effective desegregation and equal access programs are within cities where private fair housing centers have been adequately funded to address the serious problems of housing discrimination.

3. Direct financial support from HUD and federal regulators to support testing programs of the larger inter/intra-state financial institutions.

4. Development of a brochure for mortgage loan applicants explaining how to recognize subtle acts of discrimination including information on filing complaints with HUD and/or DOJ. In addition requiring lenders to provide this brochure in every applicant whose loan application is rejected or the terms or conditions of the loan altered. When a private fair housing organization operates in the area, the lender should also include that groups brochure which outlines its services.

5. All allegations of unfair lending practices received by the federal regulator would be automatically referred to HUD or DOJ.

Senator **Dixon**. Well, this has been very, very helpful. I might say that it always amazes me after a complete adult lifetime in public life that I learn something new every day at hearings of this kind.

And I must confess that, while at some place along the line, it's probably been mentioned to me, it had not occurred to me how insidiously you could design this method to avoid some of these loans by simply setting a number that excluded a good portion of our population. And I imagine that's something you all know very well. It just really had not gotten through to me until today, but I assure you that that will be a thing we'll bear in mind.

I want to say to this panel that you should not believe that because the regulators don't acknowledge the existence of it out there, that the Congress isn't aware of the fact that it exists.

We are human and we have these experiences just like you do. And we know it exists. And we are going to try to find some sensible, sane things to do about it.

Now, what we have to do here is find what we ought to do perhaps by legislation and what we ought to do working with the regulatory agencies to see that they do more. And I am concerned that they do not appear to be very strongly motivated.

Now, I get the sense that this panel, which speaks for the groups I think that are affected out there, that you're more comfortable with HUD as a place where you would get a more elevated sense of concern.

Is that a fair statement, that that is true? That the Department of Housing and Urban Development may be a more responsive agency among the regulatory agencies that were here today?

Is that a fair impression I got there? I thought you said that, Ms. Smith. I thought I sensed that maybe from Mr. Henderson.

Mr. **Henderson**. Yes, sir. I think, in comparison to the other regulatory agencies, HUD particularly under Secretary Kemp with his statement of a commitment in this area, has shown willingness and a vigor that has been lacking heretofore in the other agencies.

At the same time, I think it was particularly noteworthy——

Senator **Dixon**. That could be of course a temporary condition.

Mr. **Henderson**. I was about to——

Senator **Dixon**. Forgive me for interrupting. I don't know what the history of HUD has been in this area. I think there have been some exceptional people there who were responsive. I think of some that weren't so responsive. No offense meant to anybody.

I think all of us have a sense that Secretary Kemp is responsive in this area. What I put to you is, if we do something here responsive to what Mr. Fishbein has said by saying, Hey, put it in one place, you know, do you think we've put it in the right place if we put it there? Or is that something that you do out of heart rather than mind because of the particular individual occupying that spot?

Mr. **Henderson**. Indeed, I wanted to follow up on that observation because I noted in the statement from the HUD Assistant Secretary that there was an acknowledgment that between 1980–88, the agency had failed to monitor effectively the HMDA requirements that were imposed by law.

The fact that that reality, indeed, is confronting us now says to me that wherever we attempt to consolidate enforcement responsibilities, it has to be done with the kind of specificity that you've been aiming toward in the most recent hearings that you've held, the kind of guidance that tells the regulators precisely what we are looking for with respect to concrete data. And then the kind of oversight that ensures on a regular basis we are getting the information that is required by law.

To the extent that we can do that with a process like that which we've begun today, an open process with regulatory comment and an attempt to determine the best location for that, HUD may well be the best agency.

But I think it is also worth taking a look at the other agencies involved before making a full commitment.

Senator **Dixon**. Well, I would ask all of you to convey to us your thoughts. This is going to be an ongoing process. We didn't solve it here today. We didn't even begin to solve it here today.

I think you heard what I said. We're going to have another hearing in the spring. I think I'll let maybe six months pass and give these regulatory agencies, you know, November, December, January, February, March, April. They've got a lot of new directions on collecting raw data and other things.

Let's see what they do and what they come back with. And then, maybe about the 1st of May, we'll have you folks back and we'll have them back. And we'll put it to them and say, Now, what have you done? And give me the specificity.

And then you can say what your sense has been out there in the communities of the responsive nature of these agencies which Mr. Fishbein describes as hostile and which I say may only be not well motivated. We'll see how it turns out.

So let's try that and you folks watch it. And you all get to me your suggestions about this thing that Mr. Fishbein has talked about, and others.

Now, another thing that I was interested in because I don't quite know how you do that, Mr. Fishbein, you talked about looking into this thing at the pre-application process. It occurs to me there isn't any raw data available in a thing like that.

You've almost got to have somebody right there. I'm trying to figure out how you do that at the pre-application.

A person comes in to make a loan at the 1st National Bank of Belleville. I'll pick on a bank in my hometown. A black person comes in to make a loan. And there's this discouragement factor. Oh, we don't know, and so no encouragement, and they kind of discourage the person from pursuing the loan process much further.

How the heck do we address that? That seems like a big thing to do all over the country. I'm trying to figure it out. What do you say we ought to do about that?

Mr. **Fishbein**. Well, two things about that, Mr. Dixon.

Number one is that for a period of time, at least one of the agencies, the FDIC, required the banks it supervised to collect information about loan inquiries as well as loans actually applied for, which provided at least some information of the types of people who were asking questions.

Senator DIXON. OK, now you've got the information: Somebody came in and inquired and they didn't pursue it further.

Now what do we do?

Mr. FISHBEIN. Well, and I think that would give you information so you could compare the racial characteristics of inquiries versus loans actually applied for.

Now that has been disbanded.

Senator DIXON. Well, you get a number there, admittedly.

Mr. FISHBEIN. Right. Yes.

Senator DIXON. A thousand applications that didn't go any further than the preapplication. And 850 of those were minorities. And that says something to us, right?

Mr. FISHBEIN. I think the second technique is testing. Testing is the best method for determining whether that's a problem.

Perhaps random testing. It certainly is a big industry out there. It's very difficult to test every single institution.

Senator DIXON. You mean by testers.

Mr. FISHBEIN. By using testers. Having federal sponsorship for private agencies to do random tests to determine whether discouragement in the preapplication stage is existing.

Senator DIXON. OK.

Mr. FISHBEIN. If a program were in place, that will also have the deterrent effect on institutions to at least not discourage people on an illegal basis. Also, to have training programs in place so that their loan officers are trained in fair lending compliance.

Senator DIXON. So, simplistically, you collect all of the data on preapplication type things that don't go through and you get all those numbers, and then you do random testing of some sort. That at least—yes, I see that that could work.

Now let me ask you about this. The mortgage review boards, I get the sense that some places in the country—now Ms. Smith is pointing out, and it's the obvious reason, you know, the New York's, the California's, the Ohio's, the Illinois', the Michigan's, they do it, sure, and they've got more problems and more concern about those problems in some of their urban areas.

And then I guess she points out that a lot of places in the country, they're not doing it, which is not lost upon this chairman, I assure you.

But the point is I guess these mortgage review boards that are somewhat constituted on a voluntary basis, if my understanding of it is correct, the consumer groups working with the financial institutions kind of meet from time to time, just as Dr. Johnson and Mr. Parker worked with the Detroit banks and got a result—that sort of thing will work, won't it?

I mean, it will at least, where they do it, it will probably help some.

Ms. SMITH. It can serve a purpose. In Toledo, we've been able to negotiate agreements with a number of lenders over the last 10 years, so that whenever there is a minority or a woman's application that is rejected and it comes through our office, they share all the information with the Fair Housing Center.

So if it was based on the appraisal, we can get a copy of that appraisal report. If it was based on credit, we run the credit and find out if it was a wise decision to reject that mortgage loan.

Senator DIXON. Well, it does seem to me that, at least in the larger urban areas of the country, which I suppose we could legislatively define, and I guess I'd be compelled to observe that at least the problems we know about are more apparent there, that you could probably do something to design a way to have some kind of a voluntary effort for mortgage review boards between the community advocacy groups such as yourself and financial institutions.

And at least you would always have the jaw-boning going on there and the social awareness in the financial institutions that, hey, a problem can occur here, if you had that kind of thing in place, I think.

Mr. Parker.

Mr. PARKER. Just a comment on that.

One of the things that we have been successful with in Detroit is developing advisory boards at the various financial institutions where representatives of the community and leaders would come together with the banks at a particular bank and really discuss a large number of items, not only some mortgages but also some loan packages that they may be doing on a trial basis, and help them in marketing.

So, I think what we have done in Detroit is what needs to happen, is the coming together of those two groups, the community and the banking institutions, so they can learn from each other.

Because we have learned a lot from the financial institutions and I think they have indicated they have learned a lot from us.

Senator DIXON. Well, I'd like to hear from you all in that area, too. You know, again, one's attitudes are somewhat influenced by what one personally sees and experiences. And I know I've said before—I don't know whether I've said it in this committee, but certainly on the floor during a pretty heated debate on that question of the FHA mortgages recently—the profoundly positive impression I received from Gail Cincotta and people in Chicago that have worked to obtain more money for the communities, consumer loans and housing loans and small business loans and house improvement loans and other things.

So I think we could get from you your ideas about that.

Now I sense that your group certainly thinks that you have to separate this question with the safety and soundness business and the question of consumer compliance. That is clear.

I think, in fairness, that some of those regulators gave me the impression they're coming around to that view.

And you think that's a positive thing, Ms. Smith?

Ms. SMITH. You know, they talked about having four weeks of training on these issues and doing that, but you have to find out what constitutes their training, because even after that, they continue to find no discrimination.

Senator DIXON. Yes.

Ms. SMITH. And I don't know. I agree that it should be separated, but I think that they need to be trained by fair housing advocates, because whoever is training them in the last few years hasn't trained them on how to identify discriminatory lending practices.

Senator DIXON. Well, that's an interesting point. And we'll put that in the mix. I think that has some merit, the suggestion that it's what you train them to do that counts. Yes.

Mr. **Fishbein**. Senator Dixon, if I could follow up on Shanna's point.

We have reviewed the training programs for the different agencies. It is very important you look at specifically what these examiners are taught to do, in the effects test area is an example.

Very little time is spent on a very important area of fair lending enforcement, which is determining whether loan policies have discriminatory effects. Examiners receive only cursory training in this and very few examples about how to go about doing that.

Getting into the nitty gritty of the training program is absolutely crucial to determining whether the compliance effort is good.

Senator **Dixon**. Very good.

I would challenge each of you to put together in as abbreviated a form as you can—I don't care how much supporting documentation you have, but for the benefit of this Senator at least, I would appreciate your putting together, in each case, every one of you, your thoughts about the things that we can do to address this problem in a very straightforward and meaningful way.

Now, I warn you this Senator is not much in favor of creating a whole new set of Federal bureaucracy. I think that there are places to do this in what we have now. And I think that we can do it sensibly on the basis everything you've told me and the impressions I've gained from the regulators.

And I assure you that we will make this the kind of thing that we will pursue with some vigor. And we'll come back again in May and we'll look at it.

What I'm going to do when I have this from you is communicate that to all the regulators. And we may do some legislation as well, although I warn you that it's so late in this session that you couldn't do anything particularly meaningful I think at this late date that you could expect to get through both Houses of the Congress and to the President.

And so we are in the learning process. We are in the developmental process. But we are going to start by working with these regulators and getting back to them with some of your suggestions and some of our own that we'll share with you. And we'll begin to work on some legislation and we'll get to that. It probably will be the spring.

But I think that we will pursue really—I know we will pursue assiduously, as I said previously—this subject matter until we find sensible solutions to the problem.

And you have made a very valuable contribution and we thank you for that. And unless you have any further comments.

Dr. **Johnson**. Senator, may I?

Senator **Dixon**. Yes, Dr. Johnson.

Dr. **Johnson**. Not to be overlooked and confused in this discussion, it seems to me is that a part of safety and soundness is fairness.

Senator **Dixon**. Yes.

Dr. **Johnson**. And while we've talked about, you know, a separate operational approach getting at the problem, we want these banks to understand that we are investing in their communities and conducting their business on a fair basis is a part of safety and soundness, too.

Senator **Dixon**. Yes. I would respond further by saying that the interesting thing that I've observed is that when these financial institutions, which frankly are prodded to do so by consumer advocacy groups, have done things in these communities, the result has been a delightful result. The bottom line has been splendid. It's good business.

And so everybody makes money and everybody congratulates themselves on what a remarkable thing it is.

And so I think that what we want to do is pursue that goal and we will, and we want to do it in a careful way, and we will.

And then, in the end, I think we can get a very meaningful result that you'll all be pleased with and that the financial institutions will be inclined to cooperate with, and so will the regulators.

That is the goal of the committee, and we hope that it will be the goal that we achieve.

Is there anything else from all of you?

Dr. **Johnson**. Thank you.

Senator **Dixon**. Well, then we thank you for your remarkably important contribution.

This subcommittee stands adjourned.

[Whereupon, at 12:35 p.m., the subcommittee adjourned.]

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

ALAN GREENSPAN
CHAIRMAN

January 4, 1990

The Honorable Alan J. Dixon
Chairman
Subcommittee on Consumer and
Regulatory Affairs
Committee on Banking, Housing and
Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

Thank you for your letter of October 27 containing follow-up questions on the subject of mortgage lending discrimination.

I am concerned by your feeling that the Board was not specific enough in its report on mortgage lending discrimination submitted under section 1220 of FIRREA. I can only say that we have done our best to explain our program, review the relevant studies and discuss what conclusions we believe it would be reasonable to draw from them. We have also endeavored to make some constructive suggestions in this most difficult and sensitive area. In any event, I can assure you that we will try to be as helpful as possible to you in your inquiry.

I strongly agree that we should do everything possible to assure that all prospective borrowers are treated fairly. To this end, the Federal Financial Institutions Examination Council has recently considered several initiatives such as encouraging the formation of mortgage review boards; expanding the use of Home Mortgage Disclosure Act (HMDA) data to give financial institutions' management a clearer picture of their housing-related lending patterns; sharing information obtained from interviews with community contacts among the agencies; and continuing emphasis on education for lenders and prospective borrowers on the legal protections afforded in the consumer credit area. In addition, the Board has just adopted amendments to Regulation C, implementing provisions of FIRREA, which should enhance the usefulness of HMDA data. We will be pleased to report on the progress of all these efforts at your hearing in the spring.

The Honorable Alan J. Dixon
Page Two

Our answers to your questions are enclosed. Please let me know if I can be of further assistance.

Sincerely,

Enclosure

Chairman Greenspan subsequently submitted the following in response to written questions from Chairman Alan J. Dixon, in connection with the hearing held on October 24, 1989:

Question 1: Mortgage Review Boards: What are the logistics involved in establishing these boards? Where has the idea been tried and what have been the results? Would implementation of this idea require legislation or merely regulatory coordination?

Answer: We know of no sharply defined, widely accepted view on how mortgage review boards should be constructed or precisely how they should operate. The few that have been in operation have been essentially local in their purposes and operation and, therefore, reflect local needs and abilities. We assume this local character would, and should, be retained if these boards were more widespread.

However, we can offer a generic description of the logistics involved, which are rather simple. Mortgage review boards are generally formed by bringing together representatives of community groups and lenders to provide a "second opinion" in cases where applicants feel they have been unfairly denied credit for purchasing a home. Lenders agree, in some fashion, to make the loans approved by the board. The objective is to help assure that mortgage credit is fairly available to qualified applicants, within the parameters of safe and sound lending.

Mortgage review boards are currently active, we understand, in Massachusetts and Michigan. There may be others, as well. The Boston Mortgage Review Board has functioned since 1976 and, in 1983, the state legislature enacted a measure which calls upon cities and towns to encourage the formation of such boards. In practice, the state banking commissioner's office has acted as a primary catalyst in establishing four other regional boards. With the voluntary participation of lenders and an equal number of community representatives, the boards provide an appeals mechanism in cases where applicants believe the denial was based on the location of the property.

Under the Boston guidelines, rejected mortgage loan applicants are made aware of the appeals mechanism by means of a letter provided with the adverse action notice required by federal law, which gives prospective borrowers the specific reasons for loan denials. The boards meet on a frequent, regular basis. In each case, they review the factors that were taken into account in the lender's decision including the potential borrower's credit report and verification of employment, the property appraisal, and all other information relevant to the application. Reconsideration is handled expeditiously so that, if extension of credit is found to be warranted, buyers are able to proceed to closing of the loan on the home originally sought.

According to state banking officials and the Massachusetts Urban Reinvestment Advisory Group (MURAG) -- a community organization which has worked with the boards in an ex-officio capacity -- the boards have worked well. They point out that the vast majority of mortgage lenders in the areas the boards serve do participate, and seem supportive of the concept. Yet the number of applicants requesting review has been relatively small; in 1988, the Boston board handled only 50 appeals. The lender's original decision was reversed, as we understand it, in only approximately 7 percent of those cases. In other cases where the lender's decision was upheld, the board was sometimes able to place the loan with its member financial institutions having more flexible underwriting criteria, or other abilities enabling them to accommodate the particular loan request. Rejected applicants may, of course, arrive at the same result by approaching other financial institutions on their own, but they would incur the associated application fees -- which could mean hundreds of dollars in additional expense.

In the late 1970s, the savings bank industry in New York launched its own initiative, the Mortgage Review Fund, which was roughly similar in concept. The Fund -- an association consisting of and funded exclusively by savings banks -- reviewed rejected applicants through regional committees, and made mortgage loans that were deemed creditworthy. Promotion was handled through literature distributed at savings bank branches. According to the Savings Bank Association of New York State, the Fund was active until the early 1980s when requests for review slowed to a trickle.

The establishment of mortgage review boards in metropolitan areas could be a constructive step in promoting fair lending, and could give mortgage lenders a broader experience in dealing with lower income and minority applicants. Given the limited practical experience with the boards, though, it would seem advisable to study the idea further as the FFIEC has decided to do, especially with regard to the need for the boards as perceived by community organizations, lending institutions and state banking officials, the cost implications, and the nature of any federal support that might be desirable. At this point, we do not recommend federal legislation on the subject, as it seems to be an essentially local matter sometimes calling for unique local approaches. But we are in favor of exploring whether and how we should encourage the formation of the boards, as was decided by the FFIEC.

Question 2: Testers: What would be the best way to design a testers program? Are testers feasible only for pre-application testing? Would a testers program work best under the jurisdiction of the financial regulators or of the Department of Housing and Urban Development?

Answer: It is difficult for us to provide specific guidance in designing a testing program, since we have not used testing in our enforcement of fair lending laws. However, the general concept is rather simple - individuals who are alike in the characteristics relevant to the credit granting process (but who are different in only one respect, such as race, sex, or national origin) seek a loan as a way to "test" whether they are treated similarly by lenders. Although this type of procedure has been used widely in the area of fair housing - primarily by testing whether real estate and rental agents are discouraging minorities - to our knowledge it has rarely been used in the credit area.

Probably the only feasible use of credit testers, assuming they were deemed appropriate, would be to to assess the treatment of prospective mortgage applicants in metropolitan areas in order to determine whether racial discrimination exists at the pre-application stage of the lending process. To go beyond pre-application testing would present significant costs and other obstacles connected with arranging for testers to actually go through the mortgage decision process -- for example, the need for a verifiable credit history maintained by a third party credit bureau, an appraisal with all the costs it would entail, a contract of sale on the home being "purchased" which in all respects would appear legally binding, and underlying documents to nullify the "sale" which was purportedly being financed. Senator Hatch has introduced a legislative proposal which would call for a pilot credit testing program by the Justice Department, which presumably would explore how these issues affect the feasibility and usefulness of such a program. In lieu of that, or addition to it, the financial industry might explore the use of testing for purposes of self-regulation, similar to the self-testing program used by the National Association of Realtors. Given our lack of experience with testing, and all the uncertainties about its wisdom and workability in the credit area, we are uncertain whether, if such a program were instituted, it should be under the jurisdiction of the financial regulators or HUD. However, considerations of efficiency suggest that if the financial regulators have general responsibility for enforcing the Equal Credit Opportunity and Fair Housing Acts they should be responsible for all aspects of that enforcement.

Question 3: Separate Consumer Compliance Examiners: Not all the regulatory agencies have consumer compliance examiners who are separately trained and organized from the safety and soundness examiners. What are the key features of how your consumer examiners are trained and organized which allow for more effective enforcement and policy-making?

Answer: We have long had a team of specialized consumer compliance examiners whose training sets them apart from other commercial, trust, bank holding company and other types of examiners, and equips them to assess state member bank performance under fair lending laws and the Community Reinvestment Act. These examiners conduct a separate examination and prepare a separate report of the examination. Here are some noteworthy features of our training program:

* Generally, new examiners with 3 months' on-the-job training under the tutelage of more experienced examiners attend Consumer Affairs I, an intensive 3-week school which covers in detail the 15 relevant regulations and examination procedures. Students learn the background and requirements of fair housing and fair lending legislation, and conduct a "mock examination" to foster development of proper examination skills. After about a year of field experience, examiners attend Consumer Affairs II, a 1-week school which addresses advanced examination techniques and issues (such as credit scoring, the analysis of HMDA data, and the assignment of ratings), and concludes with an in-depth CRA case study.

* Although the schools' instructors are primarily drawn from Federal Reserve System staff, we also invite guest instructors from community groups and the banking industry to provide a broad and balanced perspective on compliance and fair lending issues.

* In addition to specialized consumer training, many compliance examiners also attend Board schools focusing on the "safety and soundness" aspect of bank regulation. They acquire an understanding of regulatory accounting, financial analysis, securities terminology and basic investment portfolio concepts, as well as the requirements of the many federal regulations governing the commercial performance of financial institutions.

* At the Reserve Bank level, seminars are held for senior examiners dealing with more difficult examination-related topics, including those of regional significance which impact fair lending and CRA enforcement.

* We have long emphasized the importance of examiner contacts with people outside the bank to learn about each community and its credit needs, as well as how each bank and its lending practices are perceived within the community. A video on how to conduct effective community contact interviews,

prepared by an interagency task force headed by a member of the Board's Community Affairs staff, is widely used within the Federal Reserve System as a teaching aide.

The separate training and organization of compliance examiners has been an integral part of the Federal Reserve System structure since 1977. With our burgeoning responsibility for consumer protection legislation, we felt it was unrealistic to expect an examiner to do a top-notch job in that area and with respect to safety and soundness examinations, as well. We believe this type of approach is essential in maintaining a cadre of professional consumer compliance examiners that is extremely knowledgeable of changing regulatory requirements, and well-prepared to handle this important and complex area of specialization.

Question 4: Improvements to Complaint Procedures: What additional steps could be taken to improve the ability of consumers to recognize discrimination and to pursue their rights to non-discrimination?

Answer: One way to help assure fair treatment is to strengthen public understanding of the process involved in obtaining a mortgage loan, and the kinds of standards to which lenders must generally adhere in extending home purchase credit. To this end, it may be useful to produce a pamphlet describing the various kinds of mortgage lenders and the types of loan products in which they typically specialize, the role of real estate agents and brokers, the role of appraisals, the general nature of underwriting criteria and how mortgage lenders make their decisions. Such a pamphlet could also provide strong encouragement to file complaints in cases where applicants believe they have unfairly been denied credit and, depending on developments in the near future, to pursue the matter with a mortgage review board. We are exploring the possibility of publishing such a pamphlet with the other agencies.

Such a pamphlet could supplement our current efforts to make consumers aware of their rights.

Under provisions of the Equal Credit Opportunity Act (ECOA) and the Fair Housing Act (FHA), financial institutions have been required for many years to display posters in their lobbies which state the bases on which discrimination in the extension of credit for housing and other purposes is prohibited by law. These posters also indicate how individuals can file a discrimination complaint with the appropriate regulatory agency. The ECOA also requires that rejected loan applicants be provided a statement of the reasons for credit denial which identifies the institution's primary regulatory agency and gives its address.

The Federal Reserve, along with the other agencies, has engaged in a vigorous consumer education campaign over the years. We have made available to the public a range of pamphlets describing the protection and remedies afforded by consumer credit laws, including one entitled "How to File a Consumer Credit Complaint," which has been in circulation since 1978. We have also worked closely with consumer organizations in their efforts to heighten awareness of consumer credit rights, and have supported various educational activities each year in connection with National Consumers Week.

THE CUYAHOGA PLAN

1101 EUCLID AVE. #402
CLEVELAND, OHIO 44115/(216)621-4525

3 November 1989

TESTIMONY FOR THE SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS REGARDING MORTGAGE LENDING AND RACE IN THE CITY OF CLEVELAND, OHIO

The Cuyahoga Plan of Ohio, Inc., a non-profit metropolitan fair housing agency serving the Greater Cleveland area, greatly appreciates the opportunity to provide written testimony to the Senate Banking Committee concerning the appearance of unfair lending practices in the City of Cleveland.

The Cuyahoga Plan was established in 1974 with a three-pronged mission: working to eliminate racial discrimination in housing, reducing levels of housing segregation, and promoting permanent patterns of residential integration. The Cleveland metropolitan area has been labeled America's second most racially segregated urban center. The Cuyahoga Plan has received local and national recognition for many of its programs designed to combat the reality of segregation, including but not limited to our Discrimination Complaint Service and our Research and Public Policy Department.

It is common knowledge that banking practices which systematically deny credit in certain neighborhoods are likely to result in neighborhood deterioration and decline. What is less commonly recognized is that residential mortgage lending, or the lack thereof, has been a major means of facilitating or denying equal housing opportunities for homebuyers of all races, and a major cause of the racially segregated landscape in metropolitan areas today. Because public policy is concerned with both fair lending and fair housing practices, we wish to share with you the results of our recent research on mortgage lending and race as well as complaints received by our office of loan denials based on race.

A. STATISTICAL STUDY OF LENDING PATTERNS:

The Cuyahoga Plan recently completed a study of mortgages used to purchase single-family homes in the City of Cleveland during 1987. The study, similar to one produced by the Cuyahoga Plan two years ago based on 1985 lending data, examined the patterns of lending activity by all types of lenders (both depository and non-depository) and by individual lenders, as they relate to racial and economic characteristics of the city's neighborhoods.[1] The Cuyahoga Plan's 1987 estimates of percent nonwhite population (an annual estimating process using birth and death statistics) and median home sales prices were used as variables in measuring race and housing economics of the city's neighborhoods. The current study draws the following conclusions:

* Increase in Low-downpayment Loans/Disinvestment by Conventional Lenders: Between 1985 and 1987 there was a 50% increase in the proportion of potentially high-risk loans made in Cleveland, i.e. loans financed with low downpayments (less than 5% of the sale price). Past research, both local and national, has termed such loans high risk since there was found to be a positive correlation between the level of low-downpayment loans and the likelihood of foreclosure. Since low-downpayment loans are government-insured/guaranteed, the increase in the percent of these loans signifies a continuing reduction of investment by conventional lenders in the City of Cleveland. In 1987, over 50% of all single-family home loans in the city were made with less than 5% downpayment.

On the East side of Cleveland, home to most of the city's Black residents, the median downpayment for all one-family mortgages was 0.0% in 1987, down from 5.0% in 1985. This represents a preponderance of "negative equity" loans, where the actual amount of downpayment is not known because the mortgage amount is greater than the sale price. Home insurance and closing costs are included in the mortgage, suggesting that the buyer could only afford the very minimum downpayment. Thus there is a significant concentration of potentially risky loans and absence of conventional lending activity on the East side. The median downpayment on the West side is 10% and for the city as a whole, 3.6%.

* Correlation to Race: There is a significant statistical correlation between the percent of government-insured low-downpayment loans and race: the greater the nonwhite population of a neighborhood, the greater the proportion of loans granted with less than 5% down. The economic level of a neighborhood is

not a predictor of percent low-downpayment loans.[8] It is the predominantly Black neighborhoods which are most threatened by lack of conventional financing, regardless of their economic class.

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[1] County Recorder data on recorded mortgages were used where mortgages could be matched to deed transfers. Not all mortgages were picked up in this process and the end result was an 80% sample. However, the studies analyzed percent market share--proportions of all loans made by individual lenders or types of lenders--which remains constant even when the numbers of loans are underreported.

This data differs from HMDA data in that the studies examined only single-family first mortgages on arms length sales, not two or more family residences, refinanced loans, home improvement loans, or loans purchased from another lender.

* Mortgage Companies Biggest Lenders: Almost half the city's 1987 recorded mortgages (47%) were made by mortgage companies, up from 31% in 1985. Mortgage companies are the leading provider of potentially high-risk low-downpayment loans. The median downpayment of all single-family loans made by mortgage companies throughout the city--whether East or West side--was 0.0%, again representing a preponderance of presumably low-downpayment, negative equity loans. Median downpayments for loans granted by commercial banks is 10.2% and for thrifts is 20.0%. There is a modest statistical correlation between market share of mortgage company loans and both the race and housing economics of a neighborhood: there is a slight tendency for mortgage companies to favor neighborhoods with a larger nonwhite population and higher median sale price.

* Commercial Banks: While mortgage company market share increased in the city between 1985 and 1987, there was a 33% decrease in loans made by commercial banks, from 15% in 1985 to 10% in 1987. And a significant number of all single-family mortgages made by all commercial banks in the city in 1987 were made by the now-ailing First Bank National, the only minority-owned depository in Cleveland. Other commercial banks had only minimal single-family mortgage investments in the city. While First Bank National invested more in the predominantly Black neighborhoods of Cleveland, the other leading banks were more likely to grant loans in White neighborhoods.

* Savings and Loans: S&Ls made 34% of the one-family mortgages in 1987, about the same market share as in 1985. There is a clear and continuing trend for thrifts to be more active in White neighborhoods than in Black neighborhoods, and only in the White portions of those neighborhoods having internally disparate racial sub-groups. While two-thirds (66%) of all loans made in the City of Cleveland were made on the city's predominantly White West Side, a disproportionate number (73%) of all thrifts' loans were made on the West Side. And while one-third (34%) of all loans made in the city were made on the predominantly Black East Side, only 27% of S&L loans were made there.

A comparison between two economically comparable Cleveland neighborhoods, one White, one Black, illustrates the point. Lee-

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[8] In the City of Cleveland there was shown to be no correlation between the estimated percent nonwhite population and housing economics as measured by median single-family home sales prices.

Miles is a middle-class East Side neighborhood with one of the highest median single-family home sales prices in the city (just under $43,000) and an estimated non-White population of 93%. Old Brooklyn is a comparable middle-class West Side neighborhood with a similar ($44,000) median sale price but an estimated non-White population of 2%. Savings institutions had a 13.1% market share of all single-family home loans made in the predominantly Black Lee-Miles neighborhood but a 40.6% market share of all such loans made in the predominantly White Old Brooklyn neighborhood.

Thrifts have not done a very satisfactory job of meeting the needs of the city's Black residents, regardless of their economic status, as measured by single-family home mortgages.

Few Loans in Economically Distressed Areas: Only 74% of the city's single-family home sales had recorded mortgages in 1987. A total absence of investment by lenders generally is a function of economics and not race. Economically distressed areas where median home sales prices are very low have both fewer sales and fewer loans in proportion to sales, while neighborhoods with high median sale price tend to have a high percentage of sales with recorded mortgages. Race is not a predictor of neighborhoods in which most of the sales had recorded loans. Those residential areas hardest hit by apparent lender disinvestment are inner city neighborhoods which are threatened by continuing deterioration without an infusion of mortgage dollars.

It should be noted that we are not alleging, on the basis of our recent study, that any lending institution clearly violated federal fair lending laws. We recognize that there are a number of actors and decisions determining who obtains mortgage loans in which neighborhoods. However, one can infer from our data that the dual and segregated context within which most homebuyers seek to borrow money to finance their home purchase may both encourage and conceal discriminatory practices.

B. OBSERVATIONS OF DISCRIMINATION COMPLAINT SERVICE IN CONCILIATING OR APPEALING COMPLAINTS OF LOAN DENIALS

The Cuyahoga Plan's Discrimination Complaint Service provides investigations and advisory service to persons who believe they are victims of unlawful housing or lending discrimination. A number of common patterns have emerged in our investigations of loan denials and we would like to share our observations concerning those experiences.

One ingredient affecting racial disparities in lending patterns relates to the selective applicability of Fannie Mae's more stringent guidelines versus the Freddie Mac guidelines that are less difficult to meet. The FRMC guidelines are flexible and subjectivity is inevitably injected into the process. However, when applicants, "but for" their race, are equally qualified to buy or build homes, yet the minority applicant is sent to the more stringent mortgage buyers, it can be a subtle and almost undetectable form of preventing that party from buying or building in an area.

This type of discrimination can be unveiled through the discovery phase of litigation, by subpoenaing six months' worth of similar applications and analyzing them by regression analysis to determine the "but for" factor. If there is a "but for" factor of race or other protected classes, then it could be determined that there is a disparate impact upon those applicants of the protected class.

Savings habits are learned behavior. The importance of savings needs to be part of the national agenda, promoted through public policy, and taught as part of our early education. There were such programs in place thirty years ago. One of our staff members vividly recalls his older sister participating in one such savings program through her school. He was eager to reach fourth grade so he could start his own account through the school, but by that point the program had been discontinued. He still holds the bank that participated in the program in very high esteem.

Despite the seemingly wide disparity between 3% and 20% downpayment, after all other associated costs are accrued, the differences between the two may amount to not much more than $1,000 to $2,000 for houses in the $30-$50,000 range.

Private Mortgage Insurers (PMIs) do not provide a list of reasons for rejection, hence, unnecessarily discouraging some applicants. Had the applicants known of the reason(s) for rejection, they might have been able to resolve the problem with a few minor adjustments. A rejectee who is just a short distance from a loan receives the same notice that someone who is two years away receives, without feedback. Typically, people who are denied mortgage loans will go out and spend their downpayments or assume more debt to assuage the traumatic news. In many cases this could be avoided if they had been encouraged by the expectation that it won't take much to get a loan soon. They may feel that they can never become homeowners or that they are years away from the loan, when in fact they may be just a few months and/or minimal information away. A very familiar retort is that "we just bought this $300/month car, but they won't give us a $250/month mortgage."

Our suggestion would be to put into effect a "what if" or "but for" summary that would give the consumer a road map of terms and conditions they have failed to meet. This type of information would be very helpful for someone denied a loan in structuring their budgets, ultimately resulting in more mortgages granted. Minorities are often not privy to the fact that there is an appeal process, or conciliatory steps, that can result in a short-term decision reversal. This is partly because they do not have access to the information networks, "the good old boy" connections that relay feedback as to the time, efforts, and steps necessary to receive the desired mortgage.

The singularly most effective and important information a prospective homebuyer can receive is a direct answer to the question, "What, if anything, can I do to get the mortgage loan that I am requesting?" Must I pay off my car or write a letter to explain that my insurance company was slow to pay or that it went out of business and did not pay my medical bill? Should I save a little more and put down 20%, thereby avoiding the PMI regulations requiring near-perfect credit? Can I liquidate assets? Drive a cab on weekends to earn more money? How many months of no "late" or "slow" payments do we need?

Few, if any, of these considerations are presented to persons denied a mortgage, yet there are often a great number of options available to them to help them obtain the desired loan. There should be a system available to report what terms and conditions could be met in order to qualify for the loan. This system could assign weighted values to each variable in order to allow a "cafeteria" type list to pick and choose from one or more variables. If the applicant is informed of terms and conditions that can be met, or decisions that can be weighed and balanced, then the ultimate result will be an educated consumer, with the information needed to make a prudent choice. If this service is made available to a customer, it will create an ingratiated and loyal patron of the lender's business.

C. POLICY IMPLICATIONS AND RECOMMENDATIONS FOR FEDERAL GOVERNMENT

1. While there are various federal regulatory agencies which supervise and examine the records of federal and state commercial banks, savings and loans, and their holding companies, there is no federal regulatory agency to supervise mortgage banks and mortgage brokers. The market share of single-family home loans made by mortgage companies increases dramatically each year, and those loans carry the most risk of potential foreclosure. It is imperative that mortgage companies be supervised and regulated by an agency with functions parallel to those which oversee the banks and thrift institutions.

2. Welcome consumer provisions of the Financial Institutions Reform Recovery and Enforcement Act (FIRREA) include for the first time some mortgage companies and the secondary lending markets under the mandates of the Home Mortgage Disclosure Act (HMDA) of 1975. Also, reporting must now include data on race, sex and income of applicants. However, while only lenders with

less than $10 million in assets are exempt from HMDA, depository institutions with less than $30 million in assets are exempt from reporting the race, sex and income of applicants. While applauding the inclusion of all types of lending institutions and the new reporting requirements in the Fair Lending Oversight and Enforcement provision of FIRREA, we urge an across-the-board application of those reporting guidelines for all lenders with at least $10 million in assets. In order to identify potential disinvestment and/or discrimination, regulators and the public should have the opportunity to scrutinize the location of all loans made by race, gender and income for all lenders having the minimal $10 million assets.

3. We were told recently by an examiner of one of the federal regulatory agencies that, in practice, they view their client to be the lending institutions they supervise, and not Congress. In that light, we are skeptical of the regulators' capacity to remain objective when examining the lenders' records for the purpose of monitoring CRA compliance. Currently it is only the federal regulators who have the capability to challenge lenders' statements that any disparity in loan rejections between White and Black applicants is based strictly on economic and not racial considerations.[8] Either the relationship between the regulatory agencies and the lenders they supervise must change, or there must be some provision permitting an impartial federal agency access to individual files for scrutiny when aggregate data reveals disparities.

4. The low number of loans made in low-moderate income neighborhoods is probably caused, at least in part, by minimum principal loan amounts required by some lenders and some private mortgage insurers. To the extent that the federal government has authority in these matters, these policies should be assessed in light of their ramifications for neighborhoods in cities such as Cleveland where the median sale price for the entire city in 1988 was a modest $37,000.

5. Incentives should be provided commercial banks and savings and loans institutions to encourage their becoming Direct Endorsement Lenders of FHA and VA mortgages. In so doing, they can improve their compliance with Community Reinvestment Act obligations while also providing better scrutiny of the dollars and deals approved than is currently happening with loans made by

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[8] The 1989 **Atlanta Journal-Constitution** study of racial disparities in loan rejections nationally found that Blacks in Cleveland were almost four times as likely as White homebuyers to be rejected for a home mortgage at area savings and loan institutions, ranking the city third worst in rejection rates among the top 50 metro areas in the nation. Lenders defend these figures by saying they reflect strictly economic considerations.

mortgage companies.

6. Given the excessive and increasing foreclosure rate for homes insured through FHA loans, the FHA must develop a better capacity for detecting unqualified buyers or fraudulent loan applications. As long as the foreclosure rate is allowed to increase, urban neighborhoods will continue to deteriorate and ultimately be destroyed, and racial segregation will be perpetuated.

7. While home loans made by mortgage companies are reviewed only infrequently now for fraud and other abuse, it is believed common for a company found guilty of misconduct to reorganize under a different name and continue operating as before. Not only should there be more aggressive monitoring of mortgage company transactions, but there should be mechanisms to prevent on-going abuse by the same personnel under a different company name.

8. Monitoring of real estate agents to measure the extent and nature of racial discrimination in housing has been valuably assisted by federal funding under such programs as the Fair Housing Initiatives Program (FHIP). Comparable monitoring of lending institutions for fair lending practices is far more complicated and costly (often requiring sufficient funds to cover downpayments and legal counsel), but it is no less essential. Legislation facilitating such investigations by municipalities and fair housing and related agencies is a worthy consideration.

9. Most urban programs established to address the needs of the low-moderate income homebuyer are funded through ever-dwindling Community Development Block Grant funds. These are vital funds which should be increased, not diminished. One particularly important service which must be increased, logically through CDBG funding, is consumer pre-purchase counseling offered by non-profit agencies or local governments serving as "disinterested" third parties. Only through such counseling will it be possible to reach the goals of increasing homeownership while also reducing numbers of foreclosures.

10. While home ownership is clearly desirable, low downpayments (<5%) have a proven causal relationship to increased incidence of default and foreclosure, and yet many Americans have little or no resources for putting more than 5% down on a home purchase. One possible explanation for lack of conventional lending in some areas is homebuyers there not having savings or choosing not to save for the requisite down payment. In the Cleveland area, neighborhoods with very similar income levels and price of housing have very different lending patterns in terms of median downpayment. The federal government could and should institute a nationwide promotion campaign through the public schools to stress the importance and the benefits of savings.

11. The secondary lending market should be encouraged to assess their impact on the issue of race as a function of lending. At the least, we encourage their on-going review and modification of their underwriting guidelines to accommodate the needs of low- and moderate-income homebuyers.

12. Similarly, private mortgage insurance companies should investigate the racial impact of their practices, at the least considering more flexible guidelines for low-moderate income buyers and neighborhoods.

13. Under the HMDA amendments, lenders have the option of providing an explanation for rejections of loan applications. We believe PMIs and other credit institutions should be required to provide specific reasons for loan rejections and conditions necessary to meet the institution's credit needs, as a fundamental right of and educational aid to the consumer.

* * *

We appreciate this opportunity to bring to your attention our findings, concerns and recommendations concerning the issue of mortgage lending and race in the City of Cleveland. We would be happy to address any questions you may have.

Respectfully submitted,

Susie Rivers

Susie M. Rivers
Executive Director

cc: Senator Howard M. Metzenbaum
Senator John H. Glenn
Congressman Dennis E. Eckart
Congressman Edward F. Feighan
Congresswoman Mary Rose Oakar
Congressman Louis Stokes
Cleveland Mayor Michael R. White

Testimony
by The National Puerto Rican Coalition, Inc.
submitted to the:
Senate Banking Committee
Subcommittee on Consumer and Regulatory Affairs
on the issue of
Discriminatory Lending Practices
8 November 1989

THE NATIONAL PUERTO RICAN COALITION --AN UMBRELLA ENTITY OF 93 ORGANIZATIONAL MEMBERS REPRESENTING THE INTERESTS OF OVER 2 1/2 MILLION PUERTO RICANS IN THE UNITED STATES -- IS PLEASED THAT THE SENATE SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS IS EXAMINING THE ISSUE OF DISCRIMINATORY MORTGAGE LENDING PRACTICES AGAINST MINORITIES AND LOW-INCOME COMMUNITIES.

SINCE 1978 NPRC HAS WORKED DIRECTLY WITH COMMUNITY GROUPS FOR THE SOCIAL, ECONOMIC AND POLITICAL ADVANCEMENT OF PUERTO RICANS IN THE U.S., AND HAS ENGAGED IN ADVOCACY, IN WASHINGTON, FOR POLICIES AND MEASURES THAT WOULD PROMOTE THAT ADVANCEMENT. NPRC HAS PROVIDED TRAINING AND TECHNICAL ASSISTANCE FOR SMALL-BUSINESS DEVELOPMENT, HOUSING AND ORGANIZATION BUILDING TO LOCAL PUERTO RICAN GROUPS IN TEN CITIES IN THE NORTHEAST AND MIDWEST. IN SIX CITIES NPRC HAS ESTABLISHED JOINT "PARTNERSHIP PROJECTS" WITH LOCAL ORGANIZATIONS AND WITH PRIVATE SECTOR SUPPORT TO CARRY OUT CONCRETE PROGRAMS FOR SMALL-BUSINESS DEVELOPMENT, NEIGHBORHOOD REVITALIZATION, HOUSING AND LOCAL ADVOCACY FOR COMMUNITY ECONOMIC DEVELOPMENT. THIS EXPERIENCE HAS VIVIDLY TAUGHT US THE IMPORTANCE OF ADEQUATE FINANCING AS A MAJOR REQUIREMENT FOR COMMUNITY DEVELOPMENT.

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THE PROBLEM OF MORTGAGE LENDING DISCRIMINATION: AN OVERVIEW

DISCRIMINATION BY FINANCIAL INSTITUTIONS AGAINST NEIGHBORHOODS WITH A SIGNIFICANT CONCENTRATION OF LATINOS (INCLUDING PUERTO RICANS) HAS BEEN A PARTICULAR PROBLEM FOR OUR COMMUNITY. RESEARCH DATA DEMONSTRATES THAT SUCH DISCRIMINATION CONSTITUTES A SIGNIFICANT IMPEDIMENT TO THE ECONOMIC DEVELOPMENT AND VIABILITY OF OUR NEIGHBORHOODS. INDEED, THE COMMUNITY DEVELOPMENT NEWSLETTER, OF THE FEDERAL RESERVE BANK OF PHILADELPHIA, "CASCADE," HAS NOTED (IN REFERRING TO THE CITY OF CAMDEN, N.J. THAT "THE MOST MAJOR [DRAWBACK TO CAMDEN'S REVITALIZATION] APPEARS TO BE A MORTGAGE MARKET THAT IS FUNCTIONING INEFFECTIVELY." (VOL. 2. #2, DECEMBER 1985) ACCORDING TO DR. MICHAEL LANG OF RUTGERS UNIVERSITY, WHO COMPLETED A MAJOR STUDY IN 1985 ENTITLED, AVAILABILITY OF MORTGAGE FUNDS IN CAMDEN, NJ, "ANALYSIS OF THE HOME MORTGAGE DISCLOSURE ACT DATA (FOR CAMDEN) SHOWS THAT THERE IS A SUBSTANTIAL DIFFERENCE IN DEPOSITORY INSTITUTION LENDING ACTIVITY BETWEEN THE COUNTY AND THE CITY." HE FOUND THAT TYPICALLY NO MORE THAN 3% OF THE FIRST MORTGAGE LOANS OF DEPOSITORY INSTITUTIONS IN CAMDEN COUNTY ARE GRANTED WITHIN THE CITY OF CAMDEN. YET, 15% OF THE COUNTY'S OWNER-OCCUPIED HOUSING UNITS ARE IN THE CITY.

NPRC MEMBERS ACROSS THE COUNTRY HAVE EXERCISED THOSE AVENUES OFFERED BY EXISTING REGULATORY PROCEDURES TO PROTEST DISCRIMINATORY LENDING PRACTICES. THE PUERTO RICAN POLITICAL ACTION COMMITTEE OF CONNECTICUT, INC. (IN COALITION WITH OTHER

COMMUNITY GROUPS), AND LA CASA DE DON PEDRO IN NEWARK NEW JERSEY, FOR EXAMPLE, HAVE PROTESTED THE EFFECTS OF SUCH PRACTICES IN THEIR STATES.

WHAT ARE THE EFFECTS OF THESE DISCRIMINATORY MORTGAGE LENDING PRACTICES?

IN MERIDEN, CONNECTICUT, PUERTO RICAN AND OTHER MINORITY RESIDENTS MUST FACE THE FRUSTRATION OF PAYING RENTS THAT ARE EQUAL TO, IF NOT GREATER THAN, MEDIAN MORTGAGE PAYMENTS. IN THE FACE OF OBSTACLES TO SECURING THE NECESSARY DOWNPAYMENT TO PURCHASE A HOUSE, MANY RESIDENTS ARE DEPRIVED OF THE OPPORTUNITY FOR HOMEOWNERSHIP. OTHERS MUST RELY ON CASH TRANSACTIONS OR ON LOW-QUALITY CREDIT FROM COMMERCIAL MORTGAGE COMPANIES. WITHOUT MORTGAGE FINANCING, LOW AND MODERATE INCOME PERSONS ARE NOT ABLE TO LIVE IN THE LOCATION OF THEIR CHOICE. WITHOUT THIS CREDIT, HOMEOWNERS ARE UNABLE TO MAINTAIN THEIR HOMES IN STANDARD CONDITION, OR TO USE EQUITY IN THEIR HOMES TO FINANCE THEIR CHILDREN'S EDUCATION, OR FOR OTHER WORTHWHILE PURPOSES.

THE FAILURE BY FINANCIAL INSTITUTIONS TO MEET THE SPECIAL CREDIT NEEDS OF LOW-INCOME AND LATINO COMMUNITIES HAS NATIONAL IMPLICATIONS AS WELL. THE USE OF AVAILABLE LOAN MONIES IN THE FINANCING OF CONDO/COOP CONVERSIONS --WITHOUT REPLACEMENT HOUSING -- EXACERBATES THE EXISTING AFFORDABLE HOUSING CRISIS.

DISCRIMINATION IN THE AREA OF MORTGAGE LENDING IS A HYDRA-HEADED ECONOMIC TERROR. IT TAKES MANY FORMS. IT IS NOT JUST THE ACTUAL DENIAL OF A LOAN. IN FACT, IT MAY TAKE THE SHAPE, AND OFTEN DOES, OF A DENIAL OF OPPORTUNITY THROUGH THE FAILURE TO PROVIDE EQUAL ACCESS TO INFORMATION. WHEN A FINANCIAL INSTITUTION, FOR EXAMPLE, FAILS TO IDENTIFY THE SPECIAL CREDIT NEEDS OF OUR COMMUNITIES, TO AGGRESSIVELY MARKET MORTGAGE LOANS IN PUERTO RICAN NEIGHBORHOODS, OR TO MAKE ACCESSIBLE TO LOW-INCOME PUERTO RICAN COMMUNITIES SPECIAL PROGRAMS WHICH ARE EASILY AVAILABLE TO A MAJORITY COMMUNITY, THIS IS DISCRIMINATION.

IN ONE JURISDICTION, FOR EXAMPLE, ONE PARTICULAR BANK WHOSE LENDING PATTERNS STRONGLY SUGGESTED IT DISCRIMINATED ON THE BASIS OF INCOME AND RACE, SPONSORED A FINANCING SEMINAR FOR MORTGAGE LOANS BUT MADE NO EFFORT TO ASSURE THAT THE LOW-INCOME/ MINORITY COMMUNITY WAS REACHED. IN ADDITION, THE SEMINAR WAS HELD IN A LOCATION WHICH IS NOT FREQUENTED BY LOW-INCOME/MINORITY PERSONS.

THIS WAS JUST ONE SMALL PART OF WHAT COMMUNITY GROUPS IN CONNECTICUT DETERMINED WAS A PATTERN AND PRACTICE OF DISINVESTMENT AND DISCRIMINATION WHICH, AS INDICATED, CAN TAKE MANY FORMS.

WHAT IS SO PERNICIOUS ABOUT THIS KIND OF DISCRIMINATORY CONDUCT IS THAT IT CONVEYS A CLEAR MESSAGE TO OUR NEIGHBORHOODS, THAT THEY ARE SOMEHOW UNWORTHY OF INVESTMENT; WHAT IS JUST AS BAD IS THAT THIS MESSAGE IS ALSO CONVEYED TO OTHER POTENTIAL LENDERS.

THUS, THE CYCLE OF DISINVESTMENT, DECAY, AND DESPAIR TAKES ROOT IN THE SOCIAL AND ECONOMIC LIFE OF OUR COMMUNITIES.

PERTINENT STUDIES

A NUMBER OF STUDIES HAVE RECENTLY BEEN CONDUCTED RELATIVE TO THIS ISSUE. THE NATIONAL PUERTO RICAN COALITION WOULD LIKE TO BRING TO THE COMMITTEE'S ATTENTION SEVERAL WHICH HAVE BEEN DONE IN JURISDICTIONS WITH HIGH CONCENTRATIONS OF PUERTO RICANS. COPIES OF THESE STUDIES ARE ATTACHED.

A. NEW YORK CITY

THE CITY UNIVERSITY'S CENTER FOR LAW AND SOCIAL JUSTICE PUBLISHED A STUDY IN NOVEMBER 1988 ENTITLED RACE AND MORTGAGE LENDING IN NEW YORK CITY: A STUDY ON REDLINING. THE AUTHORS OF THE STUDY EXAMINED CENSUS REPORTS, REPORTS FILED FOR NEW YORK CITY CENSUS TRACTS UNDER PROVISIONS OF THE HOME MORTGAGE DISCLOSURE ACT, AND DATA FOR ALL LOANS MADE BY FEDERALLY REGULATED DEPOSITORY INSTITUTIONS, COMMERCIAL BANKS AND FEDERAL SAVINGS AND LOANS. THE STUDY CONSIDERED SUCH FACTORS AS RACE AND INCOME, AS WELL AS VARIABLES SUCH AS OWNER-OCCUPANCY AND AGE OF THE HOUSING STOCK IN ANALYZING MORTGAGE LENDING PATTERNS IN NEW YORK CITY. RACE MINORITY CENSUS TRACTS WERE DEFINED AS THOSE HAVING A PREDOMINANT NON-WHITE POPULATION INCLUDING WHITE HISPANICS. THE CONCLUSIONS

ARE DISTURBING. THESE ARE:

1. CITYWIDE, A HOME MORTGAGE LOAN IS SEVEN TIMES MORE LIKELY TO BE PROVIDED TO INDIVIDUALS FROM WHITE COMMUNITIES THAN FROM PREDOMINANTLY RACIAL MINORITY COMMUNITIES.

   RACE APPEARS TO BE THE ONLY REASON FOR DISPARITIES IN LENDING PATTERNS, REGARDLESS OF INCOME, QUALITY OF HOUSING STOCK, OR AGE.

2. RACE IS A MORE SIGNIFICANT DETERMINANT OF LENDING THAN INCOME. ECONOMICALLY COMPARABLE WHITE AND MINORITY NEIGHBORHOODS HAVE DRASTICALLY DIFFERING VOLUMES OF LENDING.

   THERE IS A 2 TO 1 TO 3 TO 1 DIFFERENCE IN LENDING MADE IN WHITE AND RACIAL MINORITY CENSUS TRACTS AT THE SAME MODERATE INCOME LEVEL.

   AT THE MIDDLE INCOME LEVEL THERE IS A 3 TO 1 DISPARITY BETWEEN THE NUMBER OF LOANS AWARDED IN WHITE AND RACIAL MINORITY CENSUS TRACTS.

3. WHEN CONTROLLED FOR OWNER-OCCUPIED UNITS, THE FIGURES FOR ARE SIMILAR.
   DURING THE TWO YEAR PERIOD OF THE STUDY, MODERATE INCOME WHITE CENSUS TRACTS RECEIVED 123 LOANS PER 1000 UNITS, IN CONTRAST TO ONLY 55 LOANS PER 1000 UNITS FOR MODERATE INCOME RACIAL

MINORITY CENSUS TRACTS. THE SAME HELD TRUE FOR THOSE AT THE MIDDLE INCOME LEVEL.

4. A STRONG RELATIONSHIP EXISTS BETWEEN THE DEGREE OF NEIGHBORHOOD DECLINE AND DISINVESTMENT. THOSE JURISDICTIONS WITHIN THE CITY WITH THE HIGHEST LEVELS OF DISINVESTMENT AND ABANDONMENT ARE THOSE WHICH HAVE AN 80% RACIAL MINORITY POPULATION.

B. HARTFORD, CONNECTICUT

IN JULY OF THIS YEAR, A REPORT WAS PUBLISHED BY THE CITIZENS' RESEARCH EDUCATION NETWORK A DECADE-OLD ORGANIZATION SERVING COMMUNITY GROUPS IN HARTFORD. THIS REPORT IS ENTITLED: CHECKING OUT OF HARTFORD: BANK PRIORITIES VS. NEIGHBORHOOD NEEDS. IT SPEAKS DIRECTLY TO THE NEGATIVE IMPACT WHICH FINANCIAL DISINVESTMENT HAS HAD ON THE NORTH END OF THE CITY, AN AREA WHICH IS ROUGHLY BETWEEN 20 AND 30% HISPANIC.

ITS FINDINGS ARE SIMILAR TO THOSE FOR NEW YORK CITY. ITS MAJOR CONCLUSIONS ARE:

1. HISPANIC AND BLACK NEIGHBORHOODS ARE AWARDED FEWER THAN THE MEDIAN NUMBER OF LOANS PER RESIDENTIAL BUILDING.

2. ACCORDING TO FEDERAL HOME LOAN BANK BOARD DATA, HISPANICS APPLICANTS WERE REJECTED APPROXIMATELY 3 TIMES MORE FREQUENTLY

THAN WHITES (17% VS. 5.5%) DURING THE PERIOD 1985 TO JUNE 1988.

3. ACCORDING TO INFORMATION SUPPLIED ANNUALLY BY HARTFORD BANKS TO THE CITY'S HUMAN RELATIONS COMMISSION, HARTFORD RESIDENTS WERE DENIED MORTGAGE AND HOME IMPROVEMENT LOAN APPLICATIONS AS MUCH AS FOUR TIMES AS OFTEN AS THEY DENIED SUBURBAN APPLICANTS.

C. NEW HAVEN, CONNECTICUT

A REPORT ENTITLED RESIDENTIAL LENDING IN NEW HAVEN, CONNECTICUT (PREPARED BY ALEX MOSS AND NAOMI PORAT, SHELTER FOR THE HOMELESS WORKSHOP, YALE LAW SCHOOL/ YALE SCHOOL OF ORGANIZATION AND MANAGEMENT, APRIL 27, 1989) EXAMINES RESIDENTIAL LENDING PATTERNS IN NEW HAVEN USING POPULATION DATA FROM THE CENSUS BUREAU AND REPORTS FILED UNDER THE HOME MORTGAGE DISCLOSURE ACT (HMDA).

AGAIN, THE FINDINGS REFLECT BROAD PATTERNS OF DISCRIMINATION. THE FINDINGS HOLD TRUE REGARDLESS OF INCOME, OWNER OCCUPANCY, AND AGE OF THE HOUSING STOCK. THE AUTHORS OF THE REPORT REACHED THE FOLLOWING CONCLUSIONS:

1. THE DATA REVEALS SYSTEMATIC PATTERNS OF LENDING DISCRIMINATION AGAINST MINORITY NEIGHBORHOODS. MINORITY NEIGHBORHOODS RECEIVE 2.5 TIMES FEWER RESIDENTIAL LOANS THAN WHITE NEIGHBORHOODS. THIS IS TRUE IRRESPECTIVE OF THE TYPE OF LOAN

-- PURCHASE, HOME IMPROVEMENT, MULTIFAMILY, AND NON-OCCUPANT LOAN.

2. ALL BANKS IN THE CITY FAIL TO EQUITABLE SERVE MINORITY NEIGHBORHOODS. NONE PROVIDES MORE THAN 13% OF ITS RESIDENTIAL LOANS TO MINORITY AREAS. THOSE BANKS WHICH ARE UNITS OF LARGE REGIONAL BANKS PERFORM WORSE THAN MOST LOCAL BANKS IN TERMS OF OF REGIONAL LENDING.

3. THE PATTERN OF RACIAL DISCRIMINATION HELD CONSTANT REGARDLESS INCOME, OWNER OCCUPANCY RATES, AND AGE OF THE HOUSING STOCK. APPLICATION OF MULTIPLE REGRESSION ANALYSIS TO DATA PROVIDED BY FEDERAL REGULATORS SHOWS THAT FOR EVERY 10% INCREASE IN THE MINORITY COMPOSITION OF A CENSUS TRACT, THE TOTAL LOANS WOULD DECREASE BY 7.5% ON AVERAGE.

THE CLEAR MESSAGE CONVEYED BY THESE REPORTS IS THAT THERE IS A SERIOUS PROBLEM, AND THAT IT REQUIRES DILIGENCE BY COMMUNITIES, AND RESPONSIBLE OVERSIGHT BY PUBLIC OFFICIALS. NPRC IS PLEASED THAT THE RECENT PASSAGE OF THE FINANCIAL INSTITUTIONS REFORM, RECOVERY, AND ENFORCEMENT ACT (FIRREA) CONTAINED MODIFICATIONS TO THE HOME MORTGAGE DISCLOSURE ACT (HMDA) WHICH SHOULD MAKE MORE INFORMATION AVAILABLE AND GREATER OVERSIGHT POSSIBLE.

WE LOOK FORWARD TO WORKING WITH THE APPROPRIATE BODIES OF CONGRESS AND THE EXECUTIVE TO ENSURE THAT ALL THAT CAN BE DONE WILL BE DONE TO CORRECT EXISTING ABUSES AND REVERSE THE

CONSEQUENCES OF DISCRIMINATORY MORTGAGE LENDING PRACTICES WHICH ARE THE SUBJECT OF THIS COMMITTEE'S CURRENT DELIBERATIONS.

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